

**COMMONWEALTH OF KENTUCKY
FRANKLIN CIRCUIT COURT
DIVISION II
CIVIL ACTION NO. 13-CI-1060**

NORTON HEALTHCARE, INC.

PLAINTIFF

v.

UNIVERSITY OF LOUISVILLE

DEFENDANT

NORTON'S FIRST AMENDED COMPLAINT

Plaintiff, Norton Healthcare, Inc., f/k/a Children's Hospital ("Norton"), by counsel, for its First Amended Complaint against the Defendant, University of Louisville ("U of L"), states as follows:

NATURE OF THE ACTION

1. This dispute concerns U of L's baseless attempts to seize Norton's Kosair Children's Hospital ("KCH") from Norton unless Norton accedes to a "transformational change" in the parties' half-century-old relationship that would effectively give U of L control of Norton's hospital and prevent any non-U of L doctors from practicing at the hospital, even if those doctors are more qualified than U of L's doctors. Norton will not agree to such a change—not only is there no legal basis for it, but it would have substantial negative consequences for children in the Commonwealth and their families, who depend on KCH for the highest quality pediatric care.

2. Ironically, U of L's demand for control of KCH comes at a time when it is mired in controversy. Over the last few months alone, its School of Medicine, in unprecedented fashion, has been placed on academic probation by two of the three major accreditation bodies for medical schools; it has been publicly reported that U of L overpaid a contractor with whom

its Executive Vice President of Health Affairs, Dr. David Dunn, has close ties; made six-figure payouts to several former executives, including to the University General Counsel who reportedly had questioned expenditures backed by Dr. Dunn, in exchange for non-disparagement agreements; and a high-ranking executive of the School of Medicine was indicted for embezzlement.

3. All of this occurred after Norton brought this lawsuit on September 6, 2013. The lawsuit was a response to U of L's threat to divest Norton, the region's strongest, private, non-profit healthcare provider, of its ownership of KCH, the primary pediatric hospital in the Commonwealth, and to seize for itself Norton's hospital building and equipment. U of L's threats were and are without legal basis, but created a cloud of uncertainty that threatens to disrupt the medical care for thousands of Kentucky children and Norton's orderly ownership and operation of the region's only full service children's hospital. Norton asked this Court to declare that U of L has no legal right to carry out its threats.

4. Soon after Norton filed its complaint, the parties entered into a "tolling agreement" to facilitate settlement discussions. After nearly four months of negotiations—during which U of L concealed from Norton that its School of Medicine was being placed on academic probation—the parties reached an oral settlement agreement on Friday, January 17, 2014 (the "Settlement Agreement"), and agreed to meet in person on Tuesday, January 21 (the next business day) to execute the necessary documents. On January 20, the parties confirmed in writing the essential terms of the Settlement Agreement in emails exchanged between the parties' senior executives. Also on January 20, Norton sent U of L drafts of the Settlement Agreement and the associated documents, to be discussed and signed the following day at the scheduled meeting.

5. However, on the morning of January 21, 2014, U of L reneged on the Settlement Agreement, demanding that Norton agree to an “addendum” addressing several issues that were not part of the Settlement Agreement. U of L claimed those issues were “not in dispute from our previous discussions,” but in fact they included the very same issues that had prevented the parties from reaching an earlier agreement. As a result of U of L’s repudiation of the Settlement Agreement, the parties did not meet on January 21.

6. U of L then further repudiated the settlement agreement on January 24, 2014, claiming that the parties were “awfully close” to a settlement and that an agreement was “imminent,” but denying that an agreement was reached. U of L also falsely reported to the media that Norton had walked away from negotiations and was “threatening the very existence of all of UofL’s educational and training programs at the Health Sciences Center.” The truth, as U of L knows, is that the parties completed their negotiations on January 17, 2014, when they reached the Settlement Agreement—and despite U of L’s repudiation of the Settlement Agreement, academic probations, and the public reports of turmoil and wrongdoing within U of L, Norton expects to pay U of L approximately \$30.3 million in 2014 under the parties’ existing agreements (and certain other standard form funding agreements provided to U of L that are awaiting U of L’s approval and signature), which Norton is honoring.

7. Accordingly, Norton requests an order declaring that the parties reached a binding settlement agreement on January 17, 2014, as confirmed in writing on January 20, 2014, and ordering U of L to comply with the Settlement Agreement.

8. In the event it is found that the parties did not reach a settlement agreement, Norton requests that the Court resolve its claims for declaratory relief.

9. Norton has worked with U of L for more than half a century to provide healthcare for Kentucky children and to provide U of L with access to a first-class pediatric hospital at which its medical students, residents, and faculty may practice. In the 1980's, Norton built, at its own expense, the present KCH in downtown Louisville. Norton has spent hundreds of millions of dollars developing KCH into a preeminent institution. U of L medical students, residents, and faculty and the region's private practice and employed physicians have enjoyed practicing in the present KCH facility for nearly 30 years.

10. The long relationship between Norton and U of L has been characterized by cooperation and a shared desire to provide excellent healthcare for Kentucky children. Any prior disagreements and funding or service requests between the organizations were resolved amicably.

11. In late 2012, U of L entered into a sweeping 20-year affiliation agreement with Denver, Colorado-based hospital operator Catholic Health Initiatives ("CHI"). Under that deal, CHI took over the operation of most of U of L's University Hospital. The affiliation between U of L and CHI, which came after the Governor refused to approve a proposed merger between U of L and CHI, contemplated a future potential alliance in pediatric medicine, by giving CHI a right of first refusal with respect to any U of L "Academic Support Agreement" that comes up for renewal or U of L executes during the term of their affiliation agreement (with the exception only of the initial term of the agreement that Norton and U of L were then discussing, but expressly including any renewal term of such agreement). Neither U of L nor CHI currently operates a pediatric hospital in Kentucky.

12. Soon after it entered into its sweeping affiliation with CHI, U of L's posture toward Norton changed. U of L abandoned an executed non-binding term sheet for an updated

academic support agreement, that U of L and Norton had signed only a few months earlier after almost two years of discussions, and U of L began making increasing and unreasonable demands on Norton which were contrary to how KCH had ever operated. U of L demanded, in its own words, a “transformational change” in the historic relationship – one that would give U of L, and potentially CHI, control over KCH. U of L indicated that this was its final, non-negotiable position. When Norton did not accede, U of L issued public threats, culminating on August 27, 2013, with a purported notice of breach of the ground lease for the hospital and a threat to seize KCH and medical equipment in it for itself. According to U of L, Norton will be required to “surrender to U of L the ownership and possession of the Real Property and all Buildings and Improvements” at the KCH site. (“Notice of Breach” attached and incorporated herein as Exhibit A.)

13. U of L’s threats and Notice of Breach come close on the heels of Norton’s announcement of the commencement of a planning process for a potential affiliation with University of Kentucky (“UK”) to respond to the current and future challenges of healthcare reform and which would ensure that children in the Commonwealth, whether in Lexington, Louisville, or elsewhere, have the benefit of the best available doctors, regardless of whether they are affiliated with U of L, UK, or in private practice. U of L apparently contends that any possible future provision of services by any UK doctors at KCH is cause for Norton to forfeit ownership of the hospital itself, even before the actual planning process had even begun.

14. U of L’s threats and Notice of Breach have cast an untenable cloud of uncertainty over the operation of KCH, without any legal basis. Among other things, U of L has asserted that it may terminate Norton’s lease of the land on which Norton built its hospital (the “Ground Lease”) if Norton does not agree to an updated affiliation agreement with U of L on terms

dictated by U of L. Notwithstanding three separate requests by Norton that U of L withdraw its notice, U of L has refused to do so and the parties already have a current academic affiliation agreement and over 135 other agreements that are currently in place.

15. U of L has no legal right to threaten Norton's Ground Lease or Norton's ownership of the KCH facility and improvements. The Court should so declare for three primary reasons.

16. First, U of L is not a party to the KCH Ground Lease and thus has no right to purport to "terminate" the Ground Lease. The "Lessor" under the Ground Lease is the Commonwealth of Kentucky, represented by the Secretary of the Finance and Administration Cabinet. The Commonwealth has not asserted any breach of the Ground Lease. U of L's purported Notice of Breach is not signed by any representative of the Commonwealth and it is not evident that any representative of the Commonwealth authorized U of L's threats. The Court should declare that U of L is not a proper party to assert a breach under the Ground Lease or terminate the Ground Lease.

17. Second, in addition to U of L's lack of authority for its termination threat, there has been no breach of the Ground Lease. None of U of L's allegations about Norton's conduct or positions (which are inaccurate) would, even if true, amount to a breach of the Ground Lease. Nothing in the Ground Lease (or any other agreement) requires that Norton pay U of L the millions of dollars it is demanding or restricts Norton's ability to affiliate or collaborate with other medical groups or institutions, such as the Kentucky Children's Hospital at UK. Nor does any provision of the Ground Lease (or any other agreement) impose upon Norton a continuing obligation to have an affiliation agreement in place with U of L. The language in the Ground Lease that U of L relies upon for its allegations of breach, a recital, provides only that the

hospital will “serve the interest of and will be to the benefit of the [Commonwealth] by the availability of said new [hospital] for the programs and use of the University of Louisville’s School of Medicine.” KCH is plainly “available” for U of L’s programs and use, as demonstrated by the many U of L medical students, residents, and faculty who practice at the hospital every day. This Court should declare that this recital does not impose any legal obligations on Norton and that, even if it did, that obligation would be reasonably limited to making the hospital available to faculty, medical students, and residents at U of L’s School of Medicine, who may practice at the hospital, as they have historically, along with other doctors and professionals who provide pediatric care to the children of the Commonwealth.

18. Third, even examined on their own merits, U of L’s assertions of “breach” have no basis. Norton has not restricted U of L from providing any type of pediatric care; the financial amounts that U of L demands are not based on the parties’ agreements; and Norton’s non-binding letter of intent to begin a planning process with UK is not a breach of the Ground Lease and has not harmed U of L in any way. The proposed planning process had not even begun at the time U of L issued its Notice of Breach of the Ground Lease. Norton has explained, in a September 4, 2013 response to the Notice of Breach, both that there is no plausible basis for asserting a breach and that it is nonetheless willing to address and accommodate U of L’s concerns, but U of L has refused to withdraw its pending notice and the threats contained in it. (“Response to Notice” attached and incorporated as Exhibit B.) U of L’s claims on these points—which appear to be a mere pretext for the threatened seizure of KCH—are mistaken.

19. Accordingly, in the event it is found that the parties did not reach a settlement agreement, Norton requests that this Court dispel the uncertainty that U of L has cast KCH without any basis, by declaring that U of L has no authority to declare a breach under the Ground

Lease or to purport to terminate it. Alternatively, if this Court finds U of L has authority to declare a breach or to terminate the Ground Lease, then the Court should declare:

- a. That Norton has fulfilled all of its obligations under the Ground Lease, including any obligation to make KCH available for U of L's use; and
- b. That U of L's various assertions of breach to date are without any legal or factual basis.

20. In addition, Norton intends to abide by the parties' existing affiliation agreement. U of L, however, has threatened to terminate or non-renew that agreement and U of L has demanded that Norton enter into a radically different affiliation agreement. U of L demands a new affiliation agreement under which U of L could exclude the most qualified physicians from KCH and under which Norton would become responsible for U of L's financial performance including the consequences of U of L's financial mismanagement. As a result, this Court should declare that Norton has no obligation to enter into any affiliation agreement with U of L, and that U of L may not terminate the Ground Lease by unilaterally terminating or non-renewing the parties' affiliation agreement.

PARTIES

21. Norton is a nonprofit healthcare company formed and existing under the laws of the Commonwealth of Kentucky and located in Louisville, Kentucky.

22. U of L is a Commonwealth-supported university located in Louisville, Kentucky.

JURISDICTION AND VENUE

23. This Court maintains jurisdiction over this matter pursuant to KRS §§ 23A.010 and 418.040.

24. Franklin County is a proper venue for this action pursuant to KRS §45A.245.

FACTS

I. The Settlement Agreement.

25. Soon after this lawsuit was filed, the parties entered into a tolling agreement to stay the litigation while the parties engaged in settlement discussions. The parties extended the tolling agreement three times to facilitate further discussions.

26. The parties' initial settlement discussions focused on continuing their negotiations over an updated academic affiliation agreement to update their existing affiliation agreement (the July 1, 2008 Master Affiliation Agreement, hereinafter the "2008 Master Affiliation Agreement" attached and incorporated as Exhibit C), which they have discussed since 2010.

27. The parties engaged in exhaustive discussions during the tolling periods to negotiate an updated academic affiliation agreement, including a four-day retreat in Covington, Kentucky, attended by each party's senior executives, litigation counsel, and transactional counsel. During that time, U of L knew that it would be (or was likely to be) placed on academic probation by one of its accrediting bodies, the Liaison Committee on Medical Education ("LCME"), yet concealed that fact from Norton during the entirety of the parties' negotiations.

28. The parties were unable to reach an agreement on an updated academic affiliation agreement. On January 16, 2014, Norton met with U of L and informed U of L that after months of negotiations—and in fact years, taking into account the negotiations that occurred prior to this litigation—the parties were at an impasse and Norton did not believe that an updated academic affiliation agreement could be negotiated at that time on a mutually agreeable basis. In a letter handed to U of L's David Dunn, Norton assured U of L that it intended to continue the parties' relationship, abide by all of the parties' existing agreements including the 2008 Master Affiliation Agreement, and continue to provide extraordinary financial support to U of L:

I want to assure you that we plan to continue our relationship with UofL, continuing to build on a successful academic relationship originating over 80 years ago. It is our desire that UofL will continue to be our primary academic partner in pediatrics and we will continue to operate Kosair Children's Hospital and conduct our business through our existing 2008 Master Academic Affiliation Agreement, the more than 135 current Academic Support and other agreements, and the 1981 Ground Lease Agreement with the Commonwealth.

We will continue to provide substantial financial support to UofL, per our Academic Support Agreements and other agreements, which we expect will exceed \$27.9 million in 2014. As you know, this amount of annual support has substantially increased from the \$7.3 million that we provided in 2003 and the \$17.9 million in annual financial support that we provided in 2010. . . .

Hopefully, when the environment is less polarized in the future, there will be a time when discussions regarding an updated affiliation agreement, support agreements, and land lease agreements can be productive. At this point, however, we believe that continuing our relationship under our current agreements is the best course of action. . . .

29. During the meeting on January 16, Dr. Dunn indicated that notwithstanding the parties' inability to reach agreement on an updated affiliation agreement, U of L would be open to a global settlement of this matter if they received a lump sum financial settlement. After returning to his office later in the morning, Norton's Steve Williams telephoned Dr. Dunn to ask him to clarify what he had discussed at the breakfast meeting regarding settlement. Dr. Dunn indicated that the parties could continue to operate as they do currently if Norton paid U of L a lump sum of approximately \$10.75 million and both parties dropped their legal actions. Norton then held a meeting of the Executive Committee of its Board of Trustees on the afternoon of January 16 and again on the morning of January 17 to discuss and authorize a specific settlement proposal consistent with the parties' discussions on January 16.

30. On January 17, 2014, on a phone call between Norton's Steve Williams and Russ Cox, and U of L's David Dunn, Norton made a streamlined proposal for a global settlement

agreement, which U of L accepted. The essential terms of the Settlement Agreement, all of which were agreed to, were as follows:

- The parties agreed to continue operating under the existing 2008 Master Affiliation Agreement, as is, and roll it over into a five-year agreement beginning January 1, 2014, with auto-renewals every five years.
- Norton agreed to pay U of L a lump sum of \$10.75 million, which U of L agreed will cover all claims of any payments U of L believes Norton owes or committed to U of L. The agreed-upon amount of \$10.75 million includes approximately \$3.3 million in retroactive payments under contracts that Norton had submitted (and re-submitted) to U of L for approval, which was recently paid, and an additional approximately \$7.4 million to be used for pediatrics.
- U of L agreed to Norton's last proposal for amending the Ground Lease, and to jointly propose that amendment to the Commonwealth (the lessor under the Ground Lease) for approval. The parties agreed that the amendment would include the "sequential" process for litigation that Norton had requested, and make clear that: (a) if U of L discontinues the affiliation agreement with Norton, U of L cannot use that as basis for asserting a breach of the Ground Lease and attempt to take the hospital property; and (b) Norton must continue to make the hospital available to U of L.
- There would be nothing in any agreement that would prohibit Norton from proceeding with its letter of intent with UK, with the understanding that Norton would continue its commitment to include U of L appropriately in statewide initiatives, etc. U of L agreed to cooperate and to release its people to plan for pediatric coverage on the St. Matthews campus.
- The parties agreed to "stand down" on litigation, with U of L withdrawing the Notice of Breach, and Norton withdrawing its complaint.
- The parties extended their tolling agreement (which had expired on January 15, 2014) for 30 days to finalize the above agreements, which tolling agreement could be terminated by either party on 5 days' notice.
- The parties agreed to meet in person on January 21, 2014, with attorneys, and expedite development of the agreements.
- The parties agreed that they would then meet with State authorities as soon as possible, hopefully during the week of January 20, 2014, to seek conceptual approval of the Ground Lease amendment.

31. From January 17 through January 20, Norton prepared drafts of the Settlement Agreement and associated agreements, to be discussed and executed by the parties at January 21 meeting.

32. On January 20, in an email exchange between Mr. Williams and Dr. Dunn, the parties confirmed the essential terms of their Settlement Agreement as described above. (Ex. H, I.) Also on January 20, Norton sent U of L drafts of the Settlement Agreement and associated agreements.

33. However, on the morning of January 21, U of L repudiated the Settlement Agreement. Dr. Dunn, in phone conversations with and then an email to Mr. Williams demanded that Norton agree to an “addendum” that would address numerous additional issues that were not part of the Settlement Agreement. (Ex. J.) These issues were not discussed on January 17, not included in the parties’ written confirmation of the Settlement Agreement on January 20, and included the very same issues that prevented the parties from reaching an agreement at an earlier time.

34. After U of L repudiated the Settlement Agreement, Norton advised U of L that it would not meet as scheduled. Norton confirmed that it intended to honor the parties’ 2008 Master Affiliation Agreement and the over 135 other agreements in place between the parties.

35. On January 24, 2014, U of L’s counsel sent a letter to Norton’s counsel stating that the parties were “awfully close” to reaching an agreement, but taking the position that “not all issues were addressed or resolved.” On the same day, U of L issued a press release stating that the parties had “made major strides” towards reaching an agreement and that an agreement was “imminent,” and falsely accusing Norton of “walk[ing] away from the negotiating table” and

“threatening the very existence of all of U of L’s education and training programs at the Health Sciences Center.”

36. As U of L knows, the parties reached a Settlement Agreement on January 17 and were done negotiating. U of L also knows that Norton had done nothing to threaten U of L’s education and training programs, as Norton had confirmed that it was honoring the parties’ existing contractual arrangements (and certain new agreements that at the time were awaiting U of L’s approval and signature), under which Norton expects to pay U of L approximately \$30.3 million in 2014—despite the fact that U of L has recently been placed on academic probation by two different accrediting bodies and is mired in controversy.

II. The Ground Lease and U of L’s Notice of Breach.

A. Norton’s Agreement To Build And Operate Kosair Children’s Hospital.

37. Norton and its predecessors have operated hospitals in Louisville since 1886. Norton’s pediatric operations began as the Children’s Free Hospital, established in 1892 at 220 East Chestnut Street in Louisville. The Children’s Free Hospital later became Children’s Hospital, which became part of Norton in 1969.

38. In 1962, U of L and Children’s Hospital entered into an affiliation agreement that generally provided that U of L medical students, residents, and faculty would have privileges to practice and teach at Children’s Hospital. For more than fifty years following that 1962 agreement, through a series of new affiliation agreements, U of L and the successors of Children’s Hospital have maintained an affiliation and continue to maintain it to date. U of L and Norton currently are parties to the 2008 Master Affiliation Agreement.

39. In the late 1970’s and early 1980’s, Norton sought to build a new free-standing pediatric hospital in Louisville, the first such facility in Kentucky. U of L and the Commonwealth recognized the substantial benefits that would come from the construction of

such a facility by Norton, but wanted Norton to bear the substantial expense of construction and maintenance of the hospital.

40. In 1981, Norton entered into two relevant agreements pertaining to the proposed new facility: (a) the Ground Lease with the Commonwealth of Kentucky for approximately 2 acres of land owned by the Commonwealth at 231 East Chestnut Street in Louisville, for which Norton donated the then present value of the land; and (b) an agreement with U of L (the “1981 U of L Agreement”). A copy of the Ground Lease is attached as Exhibit D and a copy of the 1981 U of L Agreement is attached as Exhibit E.

41. The 1981 U of L Agreement generally provided that the University would recommend and obtain authorization from the Kentucky Department of Finance for the Commonwealth to execute a ground lease to Norton for the referenced land, and that upon execution of the ground lease, Norton would donate to the University a sum equal to the present value of this land, and Norton would construct a pediatric hospital at its own expense on that land.

42. Under the Ground Lease, Norton and the Commonwealth agreed that the hospital and improvements would remain the “sole property” of Norton during the term of the Ground Lease. (Ex. D ¶ 4.) The term of the Ground Lease is 99 years, with an option for an additional 50 years. (*Id.* ¶ 2.) The rent under the Ground Lease is one dollar per year, which was paid in advance for 99 years. (*Id.* ¶ 3.)

43. Nothing in the Ground Lease provides that the new hospital would be dedicated to U of L for its exclusive benefit or use. A preliminary recital in the Ground Lease observed that the new facility “will serve the interest of and will be to the benefit of the [Commonwealth of Kentucky] by the availability of said new pediatric facility for the programs and use of the

University of Louisville School of Medicine[.]” (*Id.* at 1.) A recital in the 1981 U of L Agreement similarly observed that the new hospital “will provide pediatric care, service and education benefitting the U of L Medical School and the citizens of the Commonwealth of Kentucky.” (Ex. E at 1.)

44. The 1981 U of L Agreement also provided Norton would invite a U of L representative to certain hospital board and committee meetings, and provide U of L with parking spaces at the new facility. Finally, the 1981 U of L Agreement provided that the 1962 affiliation agreement between U of L and Children’s Hospital would be “reviewed and updated,” and a “new revised Agreement [would be] executed by [Norton] and U of L.” (*Id.* ¶ 3.) As described below, the contemplated new revised affiliation agreement was executed by Norton and U of L in 2003, fulfilling Norton’s last obligation under the 1981 U of L Agreement, so that it was fully performed. Thereafter, in 2008, U of L and Norton entered into their current 2008 Master Affiliation Agreement.

45. Nothing in the 1981 U of L Agreement, the Ground Lease, or the 2008 Master Affiliation Agreement provided that the new hospital would be dedicated for U of L’s exclusive benefit or use. Furthermore, nothing in those agreements imposed on Norton any financial obligation to U of L, other than the one-time donation described above, or imposes on Norton a continuing obligation to be a party to an affiliation agreement with U of L. In fact, no such obligation existed in 1981 when the relevant agreements were executed, and effective July 1, 2014, U of L will have no obligation to even have an affiliation agreement in place with Norton in order to meet the requirements of the Accreditation Council for Graduate Medical Education (“ACGME”).

B. Norton's Construction And Operation Of Kosair Children's Hospital And Support For U Of L.

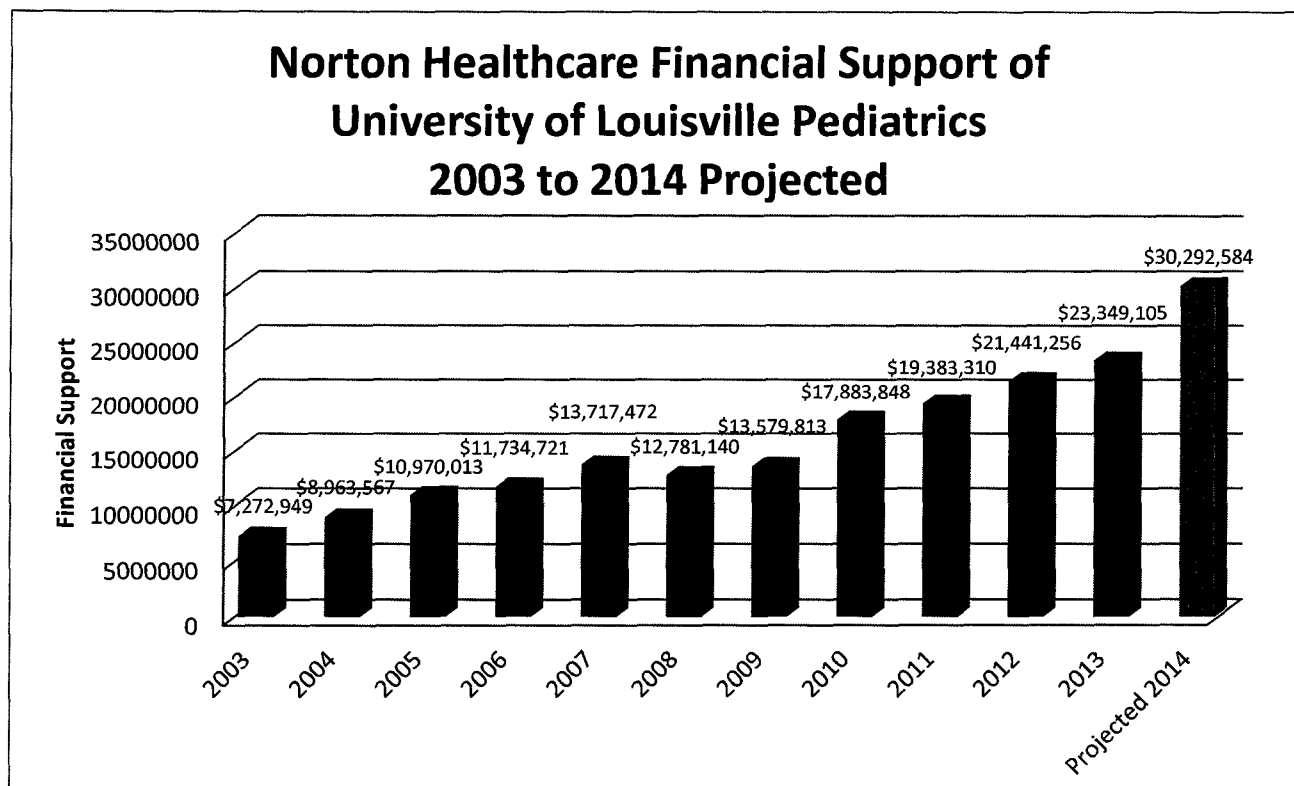
46. Following the execution of the Ground Lease, Norton constructed KCH. All told, since 1981, Norton has spent at least \$500 million on the construction, maintenance, pediatric programming, and upgrading of the facility. Norton is currently in the midst of a further \$69 million renovation project.

47. Norton has also paid for all of the high-tech medical equipment used at the hospital, in part with generous support and donations from the Louisville community. Norton has constantly upgraded this equipment as technology has improved. Those investments include tens of millions of dollars spent on equipment related to pediatric cardiac care, neonatal care, intensive care, surgical care, emergency care, diagnostic imaging, neurological disorders and cancer care, to name only a few.

48. The construction and operation of KCH has been a tremendous success for Norton, U of L, and the people of Kentucky. KCH is consistently recognized as one of the top pediatric hospitals in the nation. Kentucky families are able to obtain pediatric medical care and advanced procedures that, without KCH, would require travel to another state. The hospital, its facilities and equipment, and its culture also help attract top medical talent to Kentucky and to the U of L programs associated with the hospital.

49. Since construction of the new facility, Norton and KCH have also provided U of L with substantial financial and pediatric programmatic support, despite the fact that it was not obligated to do so under the 1981 U of L Agreement, the Ground Lease, or the 2008 Master Affiliation Agreement. As the following chart shows, the funding Norton has provided to U of L, without obligation under the 1981 U of L Agreement, the Ground Lease, or the 2008 Master Affiliation Agreement, has increased from \$7.2 million in 2003 to an expected *\$30.3 million* in

2014:



50. In 2012 alone, Norton provided U of L with more than \$21 million in financial support. Among those funds, Norton paid U of L approximately \$6.6 million in support of U of L's medical residents with the remaining amount of \$14.4 million supporting the operations of U of L's School of Medicine, Department of Pediatrics, and U of L pediatric faculty compensation. Norton has also hosted more than 100 U of L medical residents at KCH, more than any other private hospital hosts for U of L.

51. Recent events have raised serious questions about how Norton's money has been used. Over the past few months alone, it has been publicly reported that U of L overpaid a contractor with whom Dr. Dunn has close ties and made six-figure payouts to several former executives, including to the University General Counsel who reportedly had questioned

expenditures backed by Dr. Dunn, in exchange for non-disparagement agreements. Additionally, a high-ranking executive of the School of Medicine was recently indicted for embezzlement.

C. The Non-Exclusive Role of U of L at Kosair Children's Hospital.

52. Although Norton is a substantial supporter of U of L, and although U of L-employed faculty physicians, residents, and medical students perform an important role at KCH, the parties' relationship has never been exclusive.

53. Only about 30% of KCH's medical staff are employed faculty physicians of U of L. Of the doctors who admitted at least one patient to KCH in 2012, fewer than half were employed faculty physicians of U of L.

54. Over the years, Norton has entered into agreements with numerous doctors, medical groups, and institutions not affiliated with U of L for the purpose of allowing them to practice in different capacities at KCH. For example, the anesthesiologists, neonatologists, radiologists, pathologists, and orthopedic surgeons who work at KCH include (or consist solely of) non-U of L doctors. There has never been a time that U of L was the exclusive supplier of medical care at the facility.

55. Until it sought to enter into a joint venture with CHI, U of L has never before asserted that it has the right to the exclusive use of KCH and, in fact, U of L faculty have practiced side-by-side with private physicians and Norton-employed physicians for years.

D. The Parties' Negotiations And Breakdown.

56. The 2008 Master Affiliation Agreement had an initial term of one year, with an automatic renewal thereafter absent termination. The term of the 2008 Master Affiliation Agreement renewed as of July 1, 2013.

57. Although Norton is under no obligation to negotiate a new affiliation agreement, or even have an affiliation agreement in place with U of L, since 2010 Norton and U of L have

had discussions about updating the 2008 Master Affiliation Agreement and the Resident Limit Affiliation Agreement dated July 1, 2001. As part of those discussions, Norton and U of L executed a non-binding term sheet for an academic support agreement on September 28, 2012.

58. In November 2012, however, U of L announced that it had entered into a broad contractual affiliation with CHI. This contractual affiliation was reached only after the Governor refused to approve a merger between CHI and U of L. Following the Governor's rejection of the merger, U of L engaged in an "RFP" or "request for proposal" process with respect to certain opportunities to affiliate with of U of L. At the outset of that process, in a March 6, 2012 letter from U of L President Dr. Ramsey, U of L directly assured Norton that it was not necessary for Norton to respond to the RFP because U of L "commit[ted]" that the then-pending discussions about "pediatric medical and surgical programs" would "suffice for defining the relationship between Norton Healthcare and University of Louisville Pediatrics in place of responding to the Requests for Proposals."

59. U of L thereafter reached a contractual deal with CHI, in which U of L agreed that CHI would take over most of the operations of U of L's University Hospital and that U of L would acquire an ownership interest in a private CHI entity, Kentucky One, that would operate the hospital. The U of L/CHI alliance does not cover pediatric care, but the affiliation agreement between them included language suggesting a future potential affiliation in that area and purported to give CHI certain rights in that regard. As noted, neither U of L nor CHI currently operates a pediatric hospital in Kentucky.

60. Soon after U of L's affiliation with CHI, U of L began to take a dramatically different posture towards Norton and KCH. Beginning in February 2013, U of L began proposing terms for the potential new affiliation agreement with Norton that were inconsistent

with the September 2012 term sheet and that contemplated that U of L would take over control of KCH. Several of the terms U of L proposed sought to give U of L the power to prevent non-U of L doctors and groups from practicing at KCH. For example, one proposed term required Norton to maintain exclusivity for U of L in particular medical service lines. Another proposed term required exclusivity for academic training programs, which U of L said would “limit the ability of institutions other than University of Louisville to benefit from the use of Kosair Children’s Hospital.”

61. As Norton has explained to U of L, these proposed terms are not acceptable to Norton and contrary to the interests of children in the Commonwealth. There are specialized areas in which Norton must arrange for non-U of L physicians to provide care because the most qualified physician may be in private practice or affiliated with another group. Although Norton has always made KCH available for U of L’s use, including to permit hundreds of U of L residents and medical students to train at the facility, and although Norton values U of L’s contributions in providing top-quality medical services to children in many specialized areas, Norton has never agreed to operate KCH exclusively for U of L’s use or benefit and doing so would prevent Norton from providing the best possible medical care for the children of the Commonwealth. Because KCH is the primary pediatric facility in the Commonwealth, a decline in the scope or quality of service it provides would have substantial negative consequences for children in the Commonwealth.

62. That concern is even more acute today, as U of L’s School of Medicine was recently placed on academic probation by two of the three accreditation bodies for medical schools: the LCME and the Accreditation Council for Continuing Medical Education (“ACCME”). U of L is one of only two schools nationwide on probation by LCME, and the only

school to be on probation by two of the three accreditation bodies at the same time. U of L's probationary status threatens to harm the reputation of KCH for the recruitment of doctors, nurses and other medical professionals, as well as its supply of qualified residents to KCH.

63. By June 2013, U of L insisted that the "transformational change" it demanded in a new Academic Support Agreement was final and non-negotiable and threatened to discontinue an affiliation with Norton, if Norton did not capitulate. U of L has expressed the view that if Norton does not agree to U of L's dictates in relation to a new affiliation agreement, then U of L somehow has the ability to terminate Norton's Ground Lease with the Commonwealth and seize Norton's hospital and improvements.

E. U Of L's Purported Breach Notice And Threat To Terminate.

64. On August 27, 2013, U of L, by counsel, sent Norton a letter purporting to set out a "notice of default and demand for cure" under the Ground Lease. (Ex. A.) The Notice of Breach stated that it had been sent on behalf of U of L, not any representative of the Commonwealth, such as the Governor or the Secretary of Finance and Administration Cabinet (whose predecessor signed the Ground Lease on behalf of the Commonwealth).

65. U of L has no authority to terminate a Ground Lease to which the Commonwealth is a party, without express authorization from the Governor. This limit on U of L's authority was specifically recognized by the Commonwealth's Attorney General in his December 29, 2011 Report on the proposed merger between U of L and CHI (attached as Exhibit F), when U of L sought to modify other leases and affiliation agreements as part of the proposed merger. The Attorney General noted that University of Louisville Hospital was a public asset and that the Commonwealth was a party to an affiliation agreement and lease, and opined, "any modification of the Affiliation Agreement and related Ground Lease requires the approval of the Governor." (Ex. F. at 14.) Similarly, the land that is the subject of the Ground Lease to Norton is also a

public asset, and any termination of that Ground Lease necessarily also requires authorization from the Governor.

66. In its Notice of Breach, U of L purported to identify several breaches in Norton's performance under the Ground Lease. U of L claimed that, under paragraph 12 of the Ground Lease, "upon the expiration of thirty days without full and sufficient cure of such default, the 1981 Ground Lease may be forthwith terminated, and whatever ownership or possessory rights held at that time by Norton Healthcare in the Real Property, including any buildings, structures, fixtures and building equipment, together with all additions, alterations and replacements thereof . . . shall terminate." U of L further claimed that Norton must, "upon such termination, surrender to U of L the ownership and possession of the Real Property and all Buildings and Improvements." (Ex. A at 1.)

67. In other words, U of L contended that if Norton did not meet U of L's demands, U of L would seize ownership of KCH, including all of the facilities and equipment that Norton has spent hundreds of millions of dollars building and acquiring.

68. The Notice of Breach purported to identify three breaches of the Ground Lease by Norton. (Ex. A at 4 ("Norton Healthcare is in default in the prompt and full performance of the 1981 Ground Lease as the result of three separate but related actions.")) Not only was U of L not an appropriate party to assert breaches under the Ground Lease, U of L also was mistaken as to each purported breach.

F. Purported Breach No. 1: "Restricting U of L's Practice."

69. U of L first asserted that "Norton Healthcare has breached its covenant to operate Kosair Children's Hospital for the programs and use U of L's School of Medicine by unilaterally restricting U of L from providing pediatric care, teaching and research at the hospital by physicians in the pediatric specialties of anesthesiology, radiology and neurosurgery." U of L

demanded that Norton “cure this breach within thirty days by confirming in writing that in the event U of L retains credentialed physicians in these specialties, they will be granted full privileges at Kosair Children's Hospital to render care, and teach and educate students and residents.” (Ex. A at 4.)

70. U of L was mistaken in the first instance because the Ground Lease does not contain any “covenant” to operate KCH for the use of U of L, much less the exclusive use of U of L, as U of L suggested. As noted, the Ground Lease contains a preliminary recital observing that the new pediatric hospital “will serve the interest of and will be to the benefit of the [Commonwealth of Kentucky] by the *availability* of said new pediatric facility for the programs and use of the University of Louisville School of Medicine[.]” (Ex. D at 1, emphasis added.) Even if this recital imposed an affirmative duty on Norton, the only duty would be to make KCH available for the programs and use of U of L, which Norton has done since the hospital building opened.

71. U of L was also wrong factually. Norton has not “unilaterally restrict[ed]” U of L from providing care in anesthesiology, radiology and neurosurgery. In each of these specialties, Norton was required to recruit independent doctors due to problems experienced with some U of L-affiliated doctors who previously worked at KCH, in most cases with U of L’s knowledge and consent. Nonetheless, Norton confirmed in writing in its September 4 Response to Notice of Breach that that Norton would grant privileges to properly credentialed and qualified doctors that U of L employs in those fields. (Ex. B at 2.) U of L has never responded to that offer.

G. Purported Breach No. 2: Alleged Financial And Negotiation Disputes.

72. U of L next asserted in its Notice of Breach that Norton has breached the Ground Lease by: (a) failing to pay amounts purportedly due under a separate contract and failing to pay “other funding commitments” not made in any contract; (b) supposedly failing to negotiate in

good faith to amend the 2008 Master Affiliation Agreement; and (c) purportedly refusing to allow U of L representatives to attend board or executive committee meetings of Norton or KCH. (Ex. A at 4-5.) Each contention is mistaken.

73. As to the first claim, nothing in the Ground Lease—or the 1981 Agreement, or the 2008 Master Affiliation Agreement—requires Norton to pay U of L any funds. Norton has not withheld any funds from U of L, but any alleged “non-payment” of amounts due under some other agreement or commitment does not, as a matter of law, constitute a breach of the Ground Lease. Likewise, nothing in the Ground Lease requires Norton to negotiate to amend the 2008 Master Affiliation Agreement. Although Norton has negotiated in good faith for an update to that agreement, it has done so voluntarily, and any alleged failure to do so would not be a breach of the Ground Lease. Similarly, nothing in the Ground Lease, or any other agreement, requires that Norton and U of L remain parties to an affiliation agreement and in fact as of July 1, 2014 the accrediting body for Graduate Medical Education has eliminated its requirement that such an agreement even exist.

74. Moreover, even if the Ground Lease were implicated, there has been no breach. Norton is current on all amounts due to U of L under the parties’ contracts. Norton has also negotiated in good faith with respect to the affiliation agreement—the parties’ negotiations only foundered when U of L and CHI announced their new alliance (including the terms U of L granted to CHI for a future pediatric academic affiliation). With respect to U of L’s claim that it has been prevented from attending board or executive committee meetings, Norton has repeatedly confirmed in writing that U of L may attend if it wishes. (Ex. B at 3.)

H. Purported Breach No. 3: University of Kentucky Letter of Intent.

75. U of L’s last assertion of breach concerned Norton’s entry into a letter of intent with UK on August 22, 2013 (the “UK LOI”). A copy of the UK LOI is attached as Exhibit G.

76. Norton entered into the non-binding UK LOI in order to explore with UK potential collaborative efforts to improve and expand the healthcare services each organization offers in Kentucky. The focus of the contemplated relationship would be to “minimize the outmigration of pediatric care from the Commonwealth, meet the needs and interest of the Commonwealth and pediatric patients and their families and maximize the impact of the resources, programs and services of KCH and Kentucky’s Children’s Hospital” (Ex. G ¶ 1) and further benefit the citizens of the Commonwealth.

77. As Norton explained in its response to U of L’s Notice of Breach, the contemplated relationship with UK will allow U of L doctors and other qualified healthcare practitioners to provide the best medical care for children throughout the Commonwealth. (Ex. B at 3.) By increasing the network of available and qualified doctors, the relationship should also increase the flow of patients served by both U of L and UK, and as a consequence help attract top medical talent to the Commonwealth. In this era of health care reform, in which health care organizations face numerous financial and human resource challenges, this collaboration is essential to ensuring the most comprehensive and qualified medical care for the children of the Commonwealth within the resources that are available.

78. U of L asserted that the contemplated joint effort by Norton and UK would have a host of harmful effects on U of L, including the “use of Kosair Children’s Hospital in a manner that would restrict, diminish, damage, impair, and threaten the U of L School of Medicine and its Pediatric Department.” (Ex. A at 7.) U of L demanded that Norton “provid[e] adequate written assurance” that it will not “enter into any binding agreement” that would have those effects. (*Id.*)

79. U of L was again mistaken. First, nothing in the Ground Lease gives U of L exclusive rights to KCH or precludes Norton from undertaking joint efforts with other pediatric

care providers such as UK. Nothing in Norton's contemplated relationship with UK would make KCH unavailable for U of L's use. Nor would anything in Norton's contemplated relationship with UK harm U of L in any way. Indeed, the August 22, 2013 UK LOI specifically provided: "Nothing in this LOI or any agreement contemplated by it shall operate or be construed as obligating either Party to violate any explicit or implied obligations or covenants under any other agreement to which it or one of its affiliates is a party." (Ex. G ¶ 6.)

80. Second, Norton expects that any possible future relationship with UK will only benefit U of L and the overall cause of improved access to pediatric healthcare in Kentucky for the benefit of its citizens. Norton has therefore confirmed in writing that it would not enter into any agreement with UK that would delegate authority of KCH as U of L referenced in its Notice of Breach. (*See* Ex. B at 2.)

81. Finally, to the extent that U of L is deemed an arm of the Commonwealth, so too UK is an arm of the Commonwealth. And to that extent, the proposed collaboration with UK also must be deemed to have been authorized by the Commonwealth. Accordingly, U of L cannot complain that UK's agreement with Norton violates Norton's Ground Lease, because the Commonwealth will have approved both agreements.

82. Notwithstanding all of Norton's assurances, and despite three separate requests that U of L withdraw the Notice of Breach and engage in a constructive dialogue, U of L has refused to withdraw the Notice of Breach.

83. On or about September 13, 2013, by a letter dated September 10, 2013, after this lawsuit was filed, U of L and CHI amended the language in their affiliation agreement that suggested a future potential affiliation in pediatrics and purported to give CHI certain rights in that regard, so as to eliminate those rights.

CLAIMS FOR RELIEF

Count I

(Breach of Contract and Implied Covenant of Good Faith and Fair Dealing)

84. The allegations contained in Paragraphs 1 through 83 above are hereby adopted and realleged as if fully set forth herein.

85. On January 17, 2014, as confirmed in writing on January 20, 2014, the parties reached a Settlement Agreement. The essential terms of the Settlement Agreement were as follows:

- The parties agreed to continue operating under the existing 2008 Master Affiliation Agreement, as is, and roll it over into a five-year agreement beginning January 1, 2014, with auto-renewals every five years.
- Norton agreed to pay U of L a lump sum of \$10.75 million, which U of L agreed will cover all claims of any payments U of L believes Norton owes or committed to U of L. The agreed-upon amount of \$10.75 million includes approximately \$3.3 million in retroactive payments that was recently paid, and an additional approximately \$7.4 million to be used for pediatrics.
- U of L agreed to Norton's last proposal for amending the Ground Lease, and to jointly propose that amendment to the Commonwealth for approval. The parties agreed that the amendment would include the "sequential" process for litigation that Norton had requested, and make clear that: (a) if U of L discontinues the affiliation agreement with Norton, U of L cannot use that as basis for asserting a breach of the Ground Lease and attempt to take the hospital property; and (b) Norton must continue to make the hospital available to U of L.
- There would be nothing in any agreement that would prohibit Norton from proceeding with the UK LOI, with the understanding that Norton would continue its commitment to include U of L appropriately in statewide initiatives, etc. U of L agreed to cooperate and to release its people to plan for pediatric coverage on the St. Matthews campus.
- The parties agreed to "stand down" on litigation, with U of L withdrawing the Notice of Breach, and Norton withdrawing its complaint.

- The parties extended their tolling agreement (which had expired on January 15, 2014) for 30 days to finalize the above agreements, which tolling agreement could be terminated by either party on 5 days' notice.
- The parties agreed to meet in person on January 21, 2014, with attorneys, and expedite development of the agreements.
- The parties agreed that they would then meet with State authorities as soon as possible, hopefully during the week of January 20, 2014, to seek conceptual approval of the Ground Lease amendment.

86. The Settlement Agreement is a valid and enforceable contract.

87. U of L has breached the Settlement Agreement, and the implied covenant of good faith and fair dealing, by refusing to honor the Settlement Agreement and perform its obligations under it. U of L has stated that the parties were “awfully close” to a settlement, and that “an agreement was imminent,” but has claimed that “not all issues were addressed or resolved.”

88. Norton has satisfied all conditions precedent to U of L's performance under the Settlement Agreement, and stands ready, willing, and able to perform under it.

89. Norton seeks an order enforcing the Settlement Agreement and requiring U of L to perform its obligations as agreed.

90. In addition, as a direct and proximate result of U of L's breach, Norton has incurred and will continue to incur substantial damages, including continued and protracted litigation and expense. Norton is entitled to the benefit of its bargain under the Settlement Agreement, and at a minimum, to be put in the position it would have been in if U of L performed its obligations under the Settlement Agreement, including, without limitation, amending the 2008 Master Affiliation Agreement to make it a five-year term with auto-renewals every five years; jointly presenting the Ground Lease amendment to the Commonwealth for approval; and withdrawing the Notice of Default. The full amount of Norton's damages will be proven at trial.

Count II

(Declaratory Judgment)

91. The allegations contained in Paragraphs 1 through 90 above are hereby adopted and realleged as if fully set forth herein. Norton brings this claim in the alternative to Count I, in the event it is determined that the Settlement Agreement is not a valid and enforceable contract.

92. KRS 418.040 authorizes the Court to make a binding declaration of rights.

93. An actual, justiciable and present controversy exists between Norton and U of L, which requires an order declaring the rights and duties of the parties, including, but not limited to, a declaration that U of L has no authority to declare a breach under the KCH Ground Lease or to purport to terminate the Ground Lease.

94. Alternatively, if this Court finds U of L has authority to declare a breach or to terminate the Ground Lease, then this Court should declare:

- a. Norton has fulfilled all of its obligations under the Ground Lease, including any obligation to make KCH available for U of L's use; and
- b. U of L's various assertions of breach are without and legal or factual basis.

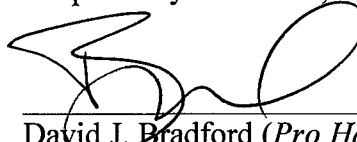
95. In addition, Norton intends to abide by the 2008 Master Affiliation Agreement. U of L, however, has threatened to terminate or non-renew that agreement and U of L has demanded that Norton enter into a radically different affiliation agreement. U of L demands a new affiliation agreement under which U of L could exclude the most qualified physicians from KCH and under which Norton would become responsible for U of L's financial performance including the consequences of U of L's financial mismanagement. As a result, this Court should declare that Norton has no obligation to enter into any affiliation agreement with U of L, and that U of L may not terminate the Ground Lease by unilaterally terminating or non-renewing the 2008 Master Affiliation Agreement.

REQUEST FOR RELIEF

WHEREFORE, Plaintiff, Norton Healthcare, Inc., respectfully requests that this Court enter judgment in its favor and grant it the following relief:

1. A declaration that U of L breached the Settlement Agreement and the implied covenant of good faith and fair dealing, and awarding Norton specific performance and all damages proximately incurred as a result of the breach.
2. In the event it is determined that the Settlement Agreement is not a valid and enforceable contract:
 - a. A declaration that U of L has no authority to declare a breach under the KCH Ground Lease or to purport to terminate the Ground Lease.
 - b. Alternatively, if this Court finds U of L has authority to declare a breach or to terminate the Ground Lease, a declaration that: (i) Norton has fulfilled all of its obligations under the Ground Lease, including any obligation to make KCH available for U of L's use; and (ii) U of L's various assertions of breach are without any legal or factual basis. The Court also should declare that Norton does not have an obligation to be a party to an affiliation agreement with U of L, and U of L may not terminate the Ground Lease by unilaterally terminating or non-renewing the 2008 Master Affiliation Agreement.
3. A trial by jury on any issues of material fact presented by the claims; and
4. All other relief to which Norton may be entitled.

Respectfully submitted,



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CERTIFICATE OF SERVICE

It is hereby certified that a copy of the foregoing was delivered via email and U.S. mail on this the 16th day of June, 2014 to:

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