

NORTON HEALTHCARE, INC.

Plaintiff

**v. UNIVERSITY OF LOUISVILLE'S ANSWER, AFFIRMATIVE DEFENSES,
AND COUNTERCLAIMS AGAINST NORTON HEALTHCARE, INC.**

UNIVERSITY OF LOUISVILLE

Defendant

* * * * *

Defendant, University of Louisville ("UofL"), states as follows for its answer, affirmative defenses, and counterclaims against Norton Healthcare, Inc. ("Norton"):

ANSWER

Nature of the Action

1. In response to the allegations in paragraph 1 of the complaint, UofL denies Norton's claim that UofL has "threatened" it, and acted "without legal basis." UofL further denies that it has "created a cloud of uncertainty that threatens to disrupt the medical care for thousands of Kentucky children and Norton's orderly administration of the hospital." To the extent there is such a "cloud of uncertainty," then Norton's conduct certainly created that "cloud." (See Counterclaim, *infra*.) UofL sent a letter dated August 27, 2013 notifying Norton of default under a 1981 lease of real property, and demanding cure of the default in addition to other claims. This letter is attached to Norton's complaint as Exhibit A. UofL denies any allegations in paragraph 1 which are inconsistent with the contents of the letter. UofL admits that Norton has covenanted that Kosair Children's Hospital shall serve as UofL's pediatric teaching hospital and that Norton administers the Kosair Children's Hospital while the UofL

School of Medicine faculty and residents provide the vast majority of the medical care and treatment at Kosair Children's Hospital. UofL lacks knowledge or information sufficient to form a belief as to the truth of the remaining allegations in paragraph 1, and therefore, denies same.

2. In response to the allegations in paragraph 2 of the complaint, UofL admits that its medical students, residents, and faculty have taught, learned, researched and provided pediatric care in the present Kosair Children's Hospital for almost 30 years. UofL also admits that it has worked in partnership with Norton to provide healthcare for Kentucky children, and to provide a first-class pediatric treatment, teaching and research hospital, in which UofL's medical students, residents, and faculty practice. In fact, UofL doctors provide medical care and treatment to the vast majority of Kentucky children at Kosair Children's Hospital. UofL lacks knowledge or information sufficient to form a belief as to the truth of the remaining allegations in paragraph 2 of the complaint, and therefore, denies same.

3. In response to the allegations in paragraph 3 of the complaint, UofL states that it has always valued its long standing public/private partnership with Norton, so that Kentucky's children receive the best possible medical care and treatment from the best trained physicians. Indeed, one of the primary purposes of the unique public/private partnership between Norton and UofL has been a desire to provide excellent healthcare for Kentucky children. But, UofL states that Norton's recent actions have threatened the long term viability of the partnership. (*See* Counterclaim, *infra*.) UofL lacks knowledge or information sufficient to form a belief as to the remaining allegations in paragraph 3, and therefore, denies same.

4. In response to the allegations in paragraph 4 of the complaint, UofL admits that neither it nor Catholic Health Initiatives ("CHI") operates a pediatric hospital in Kentucky. UofL denies the remaining allegations in paragraph 4 of the complaint.

5. In response to the allegations in paragraph 5 of the complaint, UofL denies it entered into an agreement with CHI as detailed in paragraph 4 above. UofL denies that its efforts to work with Norton to prepare a new master affiliation agreement in the months after the execution of the non-binding term sheet were anything other than reasonable and appropriate. UofL denies that it “abandoned” the terms of the non-binding term sheet, and affirmatively states that Norton took the first step in deviating from the terms of the term sheet when it provided the first draft of an affiliation agreement to UofL in October 2012, (well before any alleged agreement between UofL and CHI). UofL denies that it ever used the words “radical change” as alleged by Norton. In fact, the cover letter transmitting the most recent draft of the Master Pediatric Affiliation Agreement that UofL sent to Norton stated: “While the substance of the agreement is substantially the same ..., the format is notably different.” (June 12, 2013 Letter from Ms. Jennifer Elliott to Mr. Robert Azar, at p. 1.) UofL denies that it ever took a final, non-negotiable position in its negotiations with Norton. Rather, UofL stated: “I would suggest that we schedule a time in the next few days to discuss our revisions either in person or by phone. It may also be helpful to schedule a meeting in the very near future for our leaders to discuss the unresolved business items. This revised affiliation agreement is our final position with respect to the key outstanding business issues.” (*Id.* at p. 2.) The parties then scheduled a meeting between their respective business leaders – which Norton cancelled without explanation. Instead, Norton signed and then announced a letter of intent with another university and filed this lawsuit without having any discussions with UofL. UofL admits that its August 27, 2013 letter providing notice of default and demand for cure to Norton, is attached as Exhibit A, to Norton’s complaint. UofL denies the allegations characterizing - or purporting to paraphrase - its contents. UofL denies all

other allegations in paragraph 5 of the complaint not explicitly admitted herein, including the allegation that CHI would ever have been in a position to control Kosair Children's Hospital.

6. In response to the allegations of paragraph 6 of the complaint, UofL admits that it sent the notice of default and demand for cure letter shortly after Norton announced a joint venture letter of intent with the University of Kentucky. In fact, Norton's unilateral announcement of its intent to enter into an agreement, which among other things, would delegate and integrate joint management and operations of Kosair Children's Hospital to another university was one of the breaches that necessitated UofL's letter of August 27, 2013 providing notice of default and demanding cure. (See Complaint Exhibit A, page 7; Counterclaim, *infra*.) Norton's announcement repudiated its covenants to operate Kosair Children's Hospital—a public asset—for the programs and use of UofL School of Medicine as a pediatric teaching hospital and as a facility that was built to “provide pediatric care, service and education benefitting the UofL Medical School.” UofL also denies the last sentence of paragraph 6. Finally, UofL lacks knowledge or information sufficient to form a belief as to the remaining allegations in paragraph 6, and therefore, denies same.

7. UofL admits that it has not withdrawn the August 27, 2013 letter. UofL denies all other allegations in paragraph 7 of the complaint.

8. UofL denies the allegations in paragraph 8 of the complaint.

9. UofL denies the allegations in paragraph 9 of the complaint.

10. UofL denies the allegations in paragraph 10 of the complaint.

11. UofL admits that it has not withdrawn its notice of breach letter. UofL denies all other allegations in paragraph 11 of the complaint.

12. UofL denies the allegations in paragraph 12 of the complaint and affirmatively states that Norton is not entitled to any of its requested relief.

Parties

13. UofL admits the allegations in paragraph 13 of the complaint.

14. UofL admits that it is an agency of the Commonwealth located in Louisville, Kentucky which receives support from the Commonwealth and other sources and that under KRS 164.026 support of the University of Louisville is a public purpose for which public money may be validly expended. The remaining allegations in paragraph 14 of the complaint are denied.

Jurisdiction

15. UofL states that paragraph 15 is a legal conclusion. Regardless, UofL does not deny that this Court has jurisdiction over this matter.

16. UofL denies the allegations in paragraph 16 of the complaint.

Facts

17. UofL lacks knowledge or information sufficient to form a belief as to the truth of the allegations in paragraph 17 of the complaint, and therefore, denies same.

18. UofL admits that UofL and Children's Hospital entered into an affiliation agreement dated December 1962 which addressed a number of subjects. UofL denies Norton's allegations that attempt to paraphrase or characterize the contents of the 1962 affiliation agreement. UofL also admits that UofL and Norton are parties to a 2008 Master Affiliation Agreement which Norton has refused to update in good faith as part of its obligation to "provide care, service and education" at Kosair Children's Hospital so that UofL may continue to operate its pediatric teaching programs at Kosair Children's Hospital on terms that reflect the cost and

value of the services provided by UofL for the benefit of the patients and Norton – and for which Norton receives payments from patients, third party insurers and federal and state healthcare aid. The 2008 agreement is attached to the complaint as Exhibit C. UofL lacks knowledge or information sufficient to form a belief as to the truth of the remaining allegations in paragraph 18, and therefore, denies same.

19. UofL lacks knowledge or information sufficient to form a belief as to the truth of the allegations in the first sentence of paragraph 19 of the complaint, and therefore, denies same. UofL admits that there were substantial benefits to a partnership between UofL and Norton; in exchange for agreeing to Norton's use of UofL's land, Norton would provide for the care, service and education of pediatric patients, faculty and medical residents for the benefit of the UofL School of Medicine under an updated affiliation agreement with UofL. UofL denies the remaining allegations in the second sentence of paragraph 19 of the complaint.

20. In response to the allegations in paragraph 20 of the complaint, UofL admits that in 1981 Norton entered into a Lease with UofL as the beneficial owner of certain real property and the Commonwealth as the legal title holder "for the use and benefit of" UofL on which Norton intended to construct a new Kosair Children's Hospital facility, which consists of a Lease Agreement dated December 8, 1981 (a copy of which is attached to the Complaint as Exh. D) which "incorporated" an August 12, 1981 agreement (a copy of which is attached to the Complaint as Exh. E) "by reference" and the current affiliation agreement referred to therein concerning which Norton agreed to work with UofL to execute an updated affiliation agreement (the "Lease"). UofL denies the remaining allegations in paragraph 20 of the complaint.

21. UofL admits that the Lease addresses a number of subjects, but denies the remaining allegations of paragraph 21, which purport to characterize or paraphrase selected provisions of the Lease.

22. UofL states that a portion of paragraph 4 of the December 8 portion of the Lease states in part that the "improvements" constructed by Norton shall "at all times during the term of this Lease, and any renewal or extension thereof, remain and be the sole property of Lessee." UofL states that an advance rental payment of \$99.00 (\$1.00 per year for the initial term) was paid in advance by Norton. UofL also states that the initial term of the Lease is for 99 years and that the Lease permits the extension of the Lease for an additional 50 years on certain terms and conditions. UofL denies the remaining allegations in paragraph 22 of the complaint.

23. UofL admits that Norton covenanted in the Lease, among other things, that Norton's newly-constructed Hospital "will provide pediatric care, service and education benefitting the U of L Medical School and the citizens of the Commonwealth of Kentucky" and "will serve the interests of and will be to the benefit of the Lessor by the availability of said new pediatric facility for the programs and use of the University of Louisville's School of Medicine." UofL denies all other allegations, paraphrases and characterizations contained in paragraph 23 of the complaint.

24. UofL states that the Lease (which incorporates the referenced "1981 U of L Agreement") provides in part that Norton "agrees that the certain Affiliation Agreement between U of L and Children's Hospital dated December 12, 1962, shall be reviewed and updated by the appropriate officers of the parties hereto, and a new revised Agreement executed by NKC and U of L" and that "[t]his Agreement covers the long-standing relationship between Children's Hospital (now Kosair-Children's Hospital Division of NKC) and U of L, particularly

the Department of Pediatrics of U of L's Medical School." UofL admits that Norton agreed to a series of obligations to provide UofL transparency in connection with its operation of Kosair Children's Hospital, but denies Norton's paraphrases and characterizations of selected obligations appearing in paragraph 24. UofL admits that Norton and UofL signed affiliation agreements in 2003 and 2008, but denies that Norton has complied with its obligation under the Lease to periodically review and update the affiliation agreement in good faith. UofL denies all other allegations in paragraph 24 of the complaint.

25. UofL states that the Lease covenants require Norton to operate the Hospital as a pediatric teaching hospital for the benefit of the UofL School of Medicine and identifies no other school or entity as a beneficiary under the Lease. UofL denies all other allegations in paragraph 25 of the complaint.

26. UofL admits that Norton constructed Kosair Children's Hospital after the execution of the Lease. UofL lacks knowledge or information sufficient to form a belief as to the truth of the remaining allegations in paragraph 26 of the complaint, and therefore, denies same.

27. UofL denies that Norton "constantly upgrades" all high-tech medical equipment in Kosair Children's Hospital. UofL lacks knowledge or information sufficient to form a belief as to the truth of the remaining allegations in paragraph 27 of the complaint, and therefore, denies same.

28. UofL admits that the operation of, and care delivered through, Kosair Children's Hospital, for which UofL is jointly responsible, has successfully treated many patients over the years and has benefited the patients, their families and the community. UofL states that Kosair Children's Hospital and UofL's faculty have received certain honors and recognitions over the years and that Kosair Children's Hospital and UofL have worked together at times to attract top

medical talent to UofL programs associated with Kosair Children's Hospital. However, UofL otherwise lacks knowledge or information sufficient to form a belief as to the remaining allegations in paragraph 28, and therefore, denies same.

29. UofL admits that Norton paid UofL a total of \$20,909,894 for pediatric related clinical and administrative services provided by UofL to Kosair Children's Hospital. Such amount includes funds for academic support and \$6,461,894 for residents assigned to Kosair Children's Hospital, in 2012 and states that these payments to UofL were more than fully offset by Norton's receipt of an estimated \$32 million in federal and state funding during the same period as a result of its operation of a pediatric teaching hospital.¹ UofL states that certain of the payments alleged by Norton in paragraph 29 of the complaint do not relate to support of the pediatric teaching faculty, residents or Kosair Children's Hospital. UofL states that in the FY ended June 30, 2013, Kosair Children's Hospital hosted 100 UofL medical residents. UofL denies the allegations of paragraph 29 to the extent they imply that Norton has satisfied its Lease covenant to "provide pediatric care, service and education benefitting the U of L Medical School" and its commitments to use its federal and state funding and patient revenue to pay for shortfalls in medical education expenses, expenses associated with changing pediatric accreditation requirements, and physician hires. UofL lacks knowledge or information sufficient to form a belief as to the remaining allegations in paragraph 29, and therefore, denies same.

30. UofL denies the characterization of Norton's level of support in the first clause of paragraph 30 of the complaint, UofL admits the remaining allegations in paragraph 30.

¹ Norton received \$14,789,488 for Graduate Medical Education and Indirect Medical Education from Federal Medicare funds during the year 2012. Norton also receives an Intensity Operating Allowance Inpatient Supplement from State Medicaid funds in connection with serving as a pediatric teaching hospital. While 2012 numbers were not readily available, Norton received \$17,737,918 from State Medicaid funds for 2013 and UofL believes that amount is substantially similar to what Norton received in 2012.

31. UofL lacks knowledge or information sufficient to form a belief as to the truth of the allegations in paragraph 31 of the complaint as it is unaware of which set of statistics or data points that Norton utilized to calculate the percentages cited, and therefore, denies same.

32. UofL admits that it has not exclusively supplied *all* medical care at Kosair Children's Hospital (although it has supplied the overwhelming majority of the medical care at Kosair Children's Hospital) and states that doctors who are not UofL employees provide certain services at the Hospital. UofL lacks knowledge or information sufficient to form a belief as to the remaining allegations in paragraph 32 of the complaint, and therefore, denies same.

33. In response to the allegations in paragraph 33 of the complaint, UofL admits that it has worked with some private physicians and Norton-employed physicians at Kosair Children's Hospital. UofL denies Norton's characterization of UofL's position regarding exclusivity and any alleged relationship or agreement with CHI (*see* paragraph 4 above), and otherwise denies the allegations in paragraph 33 of the complaint.

34. UofL states that the 2008 Affiliation Agreement describes the term of the agreement as follows: "The initial term of this agreement shall be from July 1, 2008 to June 30, 2009. The agreement will thereafter be automatically renewed for one-year periods commencing on July of each year. If the agreement is not to be renewed by either party, six months' notice will be given to the other party (by January 1 of the year of termination)." UofL states that Section 11 of the 2008 Affiliation Agreement also requires "both parties" to amend both "this agreement" and "their relationship" as necessary to meet changing accreditation standards. UofL states that the agreement has been renewed automatically each year on the anniversary date, but denies that Norton has acted in good faith to update the terms of the agreement to reflect the value of the benefits Norton has received - and the increased expense load that UofL has been

required to incur – to continue to operate an accredited pediatric teaching hospital. UofL denies all other allegations in paragraph 34 of the complaint.

35. UofL admits that Norton and UofL have discussed updating and replacing the 2008 Affiliation Agreement and the 2001 Resident Limit Affiliation Agreement since 2009. UofL admits that the parties entered into a term sheet dated September 28, 2012. UofL denies all other allegations in paragraph 35 of the complaint.

36. UofL admits that at the conclusion of an RFP process on November 13, 2012, UMC, Inc., UofL, the Commonwealth of Kentucky and Kentucky One entered into certain agreements pertaining to University Hospital, not Kosair Children's Hospital. UofL states that a March 6, 2012 letter from President Ramsey stated that "We understand that affiliation agreement discussions between School of Medicine's pediatric services and Norton Healthcare are ongoing and nearing completion. This relationship is important to our pediatric medical and surgical programs and we commit that these affiliation discussions will suffice for defining the relationship between Norton Healthcare and UofL Pediatrics in place of responding to the Request for Proposals recently released regarding University of Louisville Hospital and the University of Louisville." UofL denies the remaining allegations in paragraph 36 of the complaint, including Norton's allegation that there is any agreement between UofL and CHI or that there was any proposed merger between UofL and CHI (*see* paragraph 4 above).

37. UofL admits that on November 13, 2012, UMC, Inc., UofL, the Commonwealth of Kentucky and Kentucky One entered into certain agreements pertaining to University Hospital, not Kosair Children's Hospital. UofL admits that the agreements do not cover pediatric care and that neither UofL nor CHI currently operates a pediatric hospital in Kentucky. UofL denies the remaining allegations in paragraph 37 of the complaint, including Norton's

allegation that there is any agreement between UofL and CHI (*see* paragraph 4 above) and the allegation that UofL has any ownership interest in Kentucky One. UofL states that CHI and UofL eliminated the possibility – which would have come into effect only upon and after the *termination* of Norton’s affiliation agreement with UofL - of CHI exercising any potential right of first refusal concerning a future pediatric academic affiliation agreement with UofL by a September 10, 2013 agreement amending Section 5.5(e) of the Academic Affiliation Agreement, a copy of which is attached hereto as Exhibit A.

38. UofL denies the allegations in paragraph 38 of the complaint. UofL refers to the affirmative statements in paragraphs 4 and 5 above. Further, UofL affirmatively states that ACGME requirements provide that: “One sponsoring institution must assume ultimate responsibility for the program, as described in the Institutional requirements, and this responsibility extends to resident assignments at all participating sites.” (ACGME requirements at I.A.) UofL’s position in negotiating with Norton regarding appropriate limitations on the use of Kosair Children’s Hospital was consistent with ensuring that UofL would fulfill its requirements under ACGME to operate as a qualifying program at Kosair Children’s Hospital. Norton is fully aware of these requirements as they are included in the covenants running with the 2008 master affiliation agreement between Norton and UofL.

39. UofL lacks knowledge or information sufficient to form a belief as to the truth of the allegations in paragraph 39 of the complaint pertaining to what Norton believes is acceptable to it, and therefore, denies same. UofL denies the remaining allegations in paragraph 39 of the complaint.

40. UofL admits that the Lease provides a termination remedy in the event of an uncured default, which among other remedies, would permit a surrender of the premises and

improvements thereon, and that UofL has notified Norton of a default and has demanded that Norton cure. UofL denies the remaining allegations in paragraph 40 of the complaint. Additionally, UofL refers to the affirmative statements in paragraph 5 above.

41. In response to the allegations in paragraph 41 of the complaint, UofL admits that an August 27, 2013 letter from UofL's counsel providing notice of default and demand for cure is attached to the complaint as Exhibit A, and UofL admits that it is a party signatory to the Lease and an agency of the Commonwealth. UofL denies the remaining allegations in paragraph 41 of the complaint.

42. UofL admits that the real property underlying Kosair Children's Hospital is a public asset of which UofL, as an agency of the Commonwealth, is the beneficial owner. UofL denies the remaining allegations in paragraph 42 of the complaint, including Norton's paraphrase of a document which does not mention and has no application to Kosair Children's Hospital.

43. UofL admits that the portions of paragraph 43 of the complaint that appear in quotes include selective quotations from the August 27, 2013 letter which is attached as Exh. A to the complaint. UofL denies that the letter "purports" to do anything and the remaining allegations in paragraph 43 of the complaint are denied.

44. UofL states that the August 27, 2013 letter notified Norton that the Lease provides a termination remedy in the event of an uncured default by Norton, and that an uncured default would provide UofL such a termination right and remedy. UofL denies the remaining allegations in paragraph 44 of the complaint.

45. UofL admits that the portion of paragraph 45 of the complaint that appears in quotes is a selected quotation from the August 27, 2013 letter which is attached as Exh. A to the

complaint. UofL denies the remainder of the allegations in paragraph 45, including its paraphrase thereof.

46. UofL admits that the portions of paragraph 46 of the complaint that appear in quotes include selective quotations from the August 27, 2013 letter which is attached as Exh. A to the complaint. UofL denies the remaining allegations in paragraph 46 of the complaint, including the paraphrase of the letter.

47. UofL admits that Norton covenanted in the Lease, among other things, that Norton's newly-constructed Kosair Children's Hospital "will provide pediatric care, service and education benefitting the U of L Medical School and the citizens of the Commonwealth of Kentucky" and "will serve the interests of and will be to the benefit of the Lessor by the availability of said new pediatric facility for the programs and use of the University of Louisville's School of Medicine." UofL denies all other allegations in paragraph 47 of the complaint.

48. UofL states that Norton's counsel transmitted a letter dated September 4 which stated in part that: "Nonetheless, although it has no legal obligation to do so, Norton is agreeable to U of L School of Medicine adding additional physicians to offer qualified pediatric care, teaching and/or research at Kosair Children's Hospital in these three specialties, as more fully described later in this letter," "U of L may provide services in the areas identified in your letter" and "if U of L desires to recruit qualified physicians in these areas to its full time faculty to supplement the physicians currently practicing at Kosair Children's Hospital, Norton will work with the University to that end within reasonable parameters necessary to maintain their viable medical practice and call coverage." UofL denies the remaining allegations in paragraph 48 of the complaint.

49. UofL admits that it identified certain defaults and claims in its letter of August 27, 2013, including Norton's failure to comply with the terms of the Lease as well as other contracts and commitments. UofL denies the remaining allegations in paragraph 49 of the complaint, including Norton's characterization and paraphrase of such letter.

50. UofL denies the allegations in paragraph 50 of the complaint.

51. UofL admits that Norton has "invited" UofL representatives to attend board meetings and executive committee meetings – but has rendered the "invitation" meaningless by then systematically excluding UofL from any substantive portion of the meetings which involve the Kosair Children's Hospital and its operations, as Norton's counsel admitted in the letter attached as Exh. B to the complaint. UofL denies the remaining allegations in paragraph 51 of the complaint.

52. UofL admits that the LOI is attached to the complaint as Exhibit G and that the transactions described in the LOI amount to a breach on the part of Norton. UofL denies the remaining allegations in paragraph 52 of the complaint.

53. UofL admits that Norton selectively quotes from the LOI, but lacks knowledge or information sufficient to form a belief as to the truth of the remaining allegations in paragraph 53 of the complaint, and therefore, denies same.

54. UofL states that paragraph 54 of the complaint paraphrases and characterizes a letter from Norton's lawyers which offers speculation and positions concerning the possible outcome of the LOI. UofL lacks knowledge or information sufficient to form a belief as to the truth of the allegations in paragraph 54 of the complaint, and therefore, denies same.

55. UofL admits that the August 27, 2013 letter stated in part that: "[B]y announcing its unilateral intention to enter into definitive and binding agreements that would (a) delegate

joint clinical, operational and financial control of the U of L School of Medicine's pediatric teaching hospital to a different university with a different teaching hospital; (b) use 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; and (c) delegate joint recruitment, retention and placement of pediatric specialists to a different university with a different teaching hospital, Norton Healthcare has repudiated its covenant to operate Kosair Children's Hospital — a public asset — for the programs and use of the UofL School of Medicine as its pediatric teaching hospital. See complaint Exh. G, Joint Venture Letter of Intent dated August 22, 2013. This covert plan to deprive UofL of its rights under the 1981 Lease was accomplished, in part, by Norton Healthcare's refusal to provide access to Executive Committee Meetings and Board of Directors meetings, which also constitutes a breach of the 1981 Lease, as described above.” UofL denies the remaining allegations in paragraph 55 of the complaint.

56. UofL admits that the LOI provides in part that Norton and UK “will jointly manage and engage in consolidated operations with respect to all aspects of patient care at the Hospitals, including without limitation, through joint implementation of patient care protocols, consolidated administration, joint protocols for professional and administrative staffing and personnel matters, jointly reviewing and combining approaches to supply chain, coding, billing and accounting, finance and revenue cycle programs and processes.” UofL admits that Norton selectively quotes from another provision of the LOI in paragraph 56 of the complaint. UofL denies the remaining allegations in paragraph 56.

57. UofL admits that the LOI provides in part that Norton and UK “will jointly manage and engage in consolidated operations with respect to all aspects of patient care at the Hospitals, including without limitation, through joint implementation of patient care protocols,

consolidated administration, joint protocols for professional and administrative staffing and personnel matters, jointly reviewing and combining approaches to supply chain, coding, billing and accounting, finance and revenue cycle programs and processes,” and admits that a September 4, 2013 letter from Norton’s lawyers states in part that “Norton is willing to enter into contractual commitments, as part of a global resolution of issues, to reassure U of L that Norton has no intention of delegating control of KCH to UK, as suggested in your letter. That delegation is neither contemplated by the current letter of intent nor by the parties to it.” UofL states that the LOI expressly delegates joint management and control of Kosair Children’s Hospital to another university and that the September 4 letter does not purport to change or amend the LOI. UofL lacks knowledge or information sufficient to form a belief as to the truth of the allegations in paragraph 57 concerning Norton’s actual expectations, and therefore, denies same. UofL denies the remaining allegations in paragraph 57 of the complaint.

58. UofL denies the allegations in paragraph 58.

59. UofL admits that it has not withdrawn the letter providing notice of default and opportunity to cure, nor is it obligated to do so. UofL admits that Norton has demanded that UofL withdraw the notice. UofL denies Norton’s classification of its response as containing “assurances.” UofL also denies the allegations in paragraph 59 to the extent they imply that UofL has been unwilling to engage in a constructive dialogue. UofL has been more than willing to engage in a constructive dialogue with Norton, and continues to do so. UofL denies the remaining allegations in paragraph 59 of the complaint.

Declaratory Judgment Claim for Relief

60. In response to the allegations in paragraph 60 of the complaint, UofL incorporates by reference the above answers to paragraphs 1-59 of the complaint as if fully set forth herein.

61. KRS Section 418.040 states that "In any action in a court of record of this Commonwealth having general jurisdiction wherein it is made to appear that an actual controversy exists, the plaintiff may ask for a declaration of rights, either alone or with other relief, and the court may make a binding declaration of rights, whether or not consequential relief is or could be asked." UofL denies the remaining allegations in paragraph 61 of the complaint.

62. UofL admits that an actual, justiciable and present controversy exists between Norton and UofL and denies the remaining allegations in paragraph 62 of the complaint.

63. UofL denies the allegations in paragraph 63 of the complaint.

Request for Relief

64. UofL denies that Norton is entitled to any of its requested relief.

65. UofL denies any allegations which are not otherwise expressly admitted herein.

AFFIRMATIVE DEFENSES

66. Norton's complaint fails to state a claim upon which relief can be granted.

67. Norton's complaint should be barred, in whole or in part, by waiver, estoppel, or ratification.

68. Norton's complaint should be barred by the unclean hands doctrine.

69. UofL reserves the right to assert all defenses, whether affirmative or otherwise, about which it presently lacks sufficient information, but which may become available to it during the course of this litigation.

COUNTERCLAIM

1. On August 13, 2013, after more than three years of negotiations, Norton cancelled - without explanation - a meeting scheduled for the very next day, August 14, between the business leaders of Norton and UofL. That meeting was set to finalize the terms of a Master

Affiliation Agreement which would establish and update the terms under which UofL would operate its pediatric teaching programs at Kosair Children's Hospital and Norton would pay for the care, service and education provided by UofL at the Hospital.

2. Just over a week later, on August 22, 2013, Norton issued a press release announcing that it had signed a Letter of Intent ("LOI") ceding joint operational control of Kosair Children's Hospital to a different university. Exh. G. The LOI provided in part that Norton and its new partner "will achieve clinical, operational and financial integration." The LOI explained that "[t]he Parties will *jointly manage and engage in consolidated operations* with respect to all aspects of patient care" at Kosair Children's Hospital. *Id.*, at 2. Ceding such management and control of the Hospital to a different university would serve to damage and impair UofL's pediatric teaching programs. Kosair Children's Hospital is a public asset whose mission is dedicated to serve the interests of and benefit UofL's pediatric teaching programs.

3. Norton has breached its lease obligations concerning the real property on the which Kosair Children's Hospital is sited, as well as other agreements and its fiduciary duty owed to UofL by its (1) unilateral and secret negotiation of an agreement to share joint operational control of Kosair Children's Hospital with a different university; (2) refusal to update the Master Affiliation Agreement and programmatic agreements in good faith; (3) failure to provide for care service and education at Kosair Children's Hospital; (4) actions which have eroded UofL's ability to provide pediatric teaching programs at Kosair Children's Hospital; and (5) refusals to reimburse UofL for accumulated cost deficits. These acts and omissions also give rise to causes of action for promissory estoppel and equitable relief. As a result, UofL issued a notice of default to Norton by letter dated August 27, 2013, and provided Norton an opportunity

to cure its breaches. Norton refused to withdraw the LOI and did not cure the other breaches - instead filing this pre-emptive lawsuit.

The Lease

4. UofL is the beneficial owner of a 2.2 acre tract of real property located at 231 East Chestnut Street in Louisville (the "Real Property"). The Real Property originally was the property of Jefferson County held for the use and benefit of UofL, which at the time was a city university. When UofL became part of the state university system in 1970, and thus an agency and instrumentality of the Commonwealth, the Kentucky legislature enacted a statute providing that all real property owned by or for the benefit of UofL would be titled in the name of the Commonwealth. KRS 164.870. The Real Property formed part of UofL's downtown medical campus.

The Lease formalizes a partnership between UofL and Norton.

5. In May 1981, Norton's predecessor, NKC, Inc. ("NKC" is referred to hereafter as "Norton") asked UofL if it would consider leasing the Real Property so that Norton could build a free-standing pediatric hospital to be known as Kosair Children's Hospital. At the time, the UofL School of Medicine and its Department of Pediatrics had been partners with Norton and its predecessor, Children's Hospital, for decades. The Dean of the UofL School of Medicine was a founder of Children's Hospital in the late 1800s. Norton, through one of its predecessors, became involved with Children's Hospital in 1970. UofL had been providing almost all of the physician care at Children's Hospital and UofL's faculty served in several integral roles at Children's Hospital—including as the Chief of Pediatrics, Chief of Surgery and the Chief of Staff for the hospital from its inception in the late 1800s up through the time of Norton's request in 1981 to lease the Real Property from UofL to form a new Kosair Children's Hospital which

would replace Children's Hospital. Children's Hospital served as the pediatric teaching hospital for UofL.

6. The creation of a free-standing Kosair Children's Hospital resulted from a series of agreements between Norton and Kosair Charities. For its part, Kosair Charities had a long history of successful fund-raising and serving the community through its operation of Kosair Crippled Children's Hospital located on Eastern Parkway for many years. Kosair Crippled Children's Hospital had a license for roughly one hundred (100) pediatric beds at that location. For its part, Norton's Children's Hospital had insufficient space to expand and limited pediatric beds under license – and had been losing money for a number of years. The 1981 Lease with UofL followed a series of agreements between Kosair Charities and Norton which addressed Kosair's financial investment, board seats for Kosair, use of Kosair's name and the re-location of the Eastern Parkway operations downtown along with a transfer of the 100 licensed beds to the newly-formed Kosair Children's Hospital.

7. Following Norton's new agreements with Kosair in 1981, UofL agreed to a long-term lease of UofL's Real Property to continue and expand the long-term partnership between Norton and UofL, and in exchange for a series of covenants provided by Norton.

The Lease ties together three agreements.

8. The lease between UofL as the beneficial owner, the Commonwealth as legal title holder for UofL's "use and benefit" - as provided for by KRS 164.870 - and Norton, consists of a December 8, 1981 agreement (attached hereto as Exh. B) which incorporates in full an August 12, 1981 agreement (attached hereto as Exh. C)("which Agreement, incorporated herein by reference, shall survive the execution of this Lease"), and refers to the terms of an Affiliation Agreement (affiliation agreement in place as of 1981 is attached hereto as Exh. D)("1962 Master Affiliation Agreement") between the UofL School of Medicine and Norton (collectively, the first

two agreements, coupled with the current version of the affiliation agreement, referred to generally as the "Master Affiliation Agreement" or collectively as the "Master Affiliation Agreements" form the "Lease"). As a result, the Lease ties together Norton's receipt of the leasehold interest from UofL with Norton's continuing obligation to operate Kosair Children's Hospital as UofL's affiliated pediatric teaching hospital for the term of the Lease.

UofL is both the beneficial owner of the leased property and a signatory.

9. The Lease includes UofL as a party and signatory, identifies the Real Property as "owned by UofL," and describes Norton's intent to lease the Real Property "from UofL." (Exh. B at 1, 4.) The Lease includes the Commonwealth, the legal title holder "for the use and benefit" of UofL, as a party and signatory. (Exh. C at 1, 10.)

The new facility must be operated to the "benefit" of – and "in the interest of" – the UofL School of Medicine & Norton agrees to "provide" pediatric care, service and education.

10. The Lease includes what is described as a series of "mutual covenants" between the parties. (Exh. B at 2.) Norton, for its part, covenants that the newly-constructed facility, Kosair Children's Hospital, "will provide pediatric care, service and education benefitting the UofL Medical School and the citizens of the Commonwealth of Kentucky." (Exh. B at 1.) Norton also covenants that the new Kosair Children's Hospital "will serve the interests of and will be to the benefit of the Lessor by the availability of said new pediatric facility for the programs and use of the University of Louisville's School of Medicine." (Exh. C at 1.) These covenants create a partnership between Norton and UofL to benefit "the mutual interests and benefit of the parties hereto, in the conduct of their respective programs." (Exh. B at 1.)

Norton must maintain and update a Master Affiliation Agreement with UofL – without which UofL cannot operate pediatric teaching programs.

11. The partnership established by the Lease covenants is supported by Lease provisions which require Norton, among other things, to update and maintain an affiliation

agreement for UofL's pediatric teaching hospital and provide UofL a measure of transparency concerning Kosair Children's Hospital's plans and operations. The Lease includes Norton's agreement that the existing 1962 Master Affiliation Agreement "shall be reviewed and updated by the appropriate officers of the parties hereto, and a new revised Agreement executed by NKC and UofL." (Ex. A at 2-3.) This makes good sense. UofL cannot maintain accreditation for pediatric teaching programs unless it has a current updated Master Affiliation Agreement in place with Kosair Children's Hospital. ACGME Institutional Requirements (eff. July 1, 2007). ACGME accreditation standards require that all Master Affiliation Agreements be reviewed, amended and renewed regularly to take into account changes in pediatric program requirements, at least every five (5) years. *Id.*, § I.C.2. And if UofL loses accreditation, it loses the ability to operate a pediatric teaching program. The Lease explains that the Master Affiliation Agreement "covers the long-standing relationship between Children's Hospital (now Kosair-Children's Hospital Division of NKC) and UofL, particularly the Department of Pediatrics of U of L's Medical School." (*Id.* at 3.)

"Provide" means "pay."

12. The Master Affiliation Agreements, through programmatic affiliation agreements referred to therein (which incorporate the terms of the Master Affiliation Agreements), are intended to address the amounts which Norton is required to pay to satisfy its Lease covenant "to *provide* pediatric care, service and education benefitting the UofL Medical School." (Ex. C at 4.) (emphasis supplied) The parties have always considered Norton's obligation to "provide" care, service and education to include *paying* UofL for services provided at Kosair Children's Hospital. UofL sustains an annual deficit for providing such care – and Norton receives patient/insurer funds and government aid which is available to pay UofL for the services it

provides. Further, Norton has affirmed its obligation to periodically update the Master Affiliation Agreement. These updates address changes in accreditation standards and plans for compliance, in addition to paying for UofL's increased costs of providing such care, service, and education at Kosair Children's Hospital. (*Id.*) In the Master Affiliation Agreements executed in 2003 and 2008, Norton "acknowledges that the University in training students operates under the specific standards of the Liaison Committee for Medical Education ('LCME') and that these standards are both obligatory for the University and subject to periodic modification; and . . . that the University in training residents operates under the specific standards of the Accreditation Council for Graduate Medical Education ('ACGME') and its specialty-based Residency Review Committees ('RRC's') and that standards from these bodies are both obligatory for the University and subject to periodic modification." (Exh. D at 1.) Without a Master Affiliation Agreement, UofL would be unable to operate pediatric teaching programs at Kosair Children's Hospital. As a result of the fact that UofL's cost of providing pediatric care, service and education increase as a result of such changes, the Master Affiliation Agreements require Norton and UofL "to amend this agreement and their relationship as necessary to meet changing accreditation standards applicable to each party." (*Id.* at 4.)

13. Each Master Affiliation Agreement "acknowledges that programmatic affiliation agreements between each residency specialty program and NHC are required by the ACGME and will work to implement and maintain such agreements." (*Id.*) The parties acknowledged that "additional specific other agreements" would cover "specific programs between the two organizations." (*Id.*) The parties also agreed to "negotiate resident stipends and benefits annually, with both parties agreeing to make annual adjustments so that resident stipends and benefits are competitive based on regional benchmarking." (*Id.* at 6.)

Norton owes UofL a duty of transparency and communication under the Lease.

14. Because UofL granted a 99-year lease of its Real Property for a pediatric teaching hospital, and Norton in exchange has covenanted to operate Kosair Children's Hospital to "serve the interest of" - and "for the benefit of" - UofL's School of Medicine (Exh. C at 1), Norton is not a mere contracting party, but a partner with certain duties of transparency, communication and disclosure. The Lease requires Norton to permit UofL representatives to be invited to attend not only meetings of its Board of Directors - but also meetings of its Executive Committee - in order "to assure full and open communication between them." (Exh. B at 2.)

The Critical Care Agreement.

15. As required by the Lease and the Master Affiliation Agreements referred to therein and made a part thereof, Norton entered into several programmatic affiliation agreements with UofL, including the Agreement for the Provision of Critical Care and Sedation Services (Exh. E)(also referred to as the "Critical Care Agreement"). The Master Affiliation Agreements provide that their terms are "intended to be additive" to the individual programmatic affiliation agreements, including the Critical Care Agreement. (Complaint Exh. C at 2.)

16. Under the Critical Care Agreement, as renewed at the close of each term, Norton agreed to pay compensation for various critical care services, as set forth in Attachment D to that Agreement. Among other items, the Critical Care Agreement required that Norton pay a group guarantee which was based on an Income Guarantee formula. The formula includes factors such as the number of full-time equivalent physicians ("FTEs"), account net revenue and total operating expenses. (Exh. E at Attachment D.)

17. Because of changes in resident duty hour limits mandated by the ACGME, the availability of resident staffing for patient care activities in the Critical Care Unit at Kosair Children's Hospital has been reduced. In addition, UofL's cost of providing patient care at

Kosair Children's Hospital has increased as a result of increases in patient acuity and increases in market compensation for physicians. These factors required UofL to recruit and hire additional faculty physicians in order to provide needed patient care and to meet ACGME-mandated resident supervision requirements. In doing so, UofL must also increase existing physician faculty compensation to meet the level of compensation required for new hires.

18. Both the Master Affiliation Agreements ("both parties agree to amend this agreement and their relationship as necessary to meet changing accreditation standards") (Complaint Exh. D at 4) and the Critical Care Agreement (Exh. E, Attachment D) (requires Norton to "negotiate [FTEs] in good faith" adjustments at the end of each contract term) require Norton to increase its level of support to reimburse UofL for increased costs resulting from changes in accreditation requirements.

Norton Receives Federal and State Funding for its Operation of Kosair Children's Hospital as a Pediatric Teaching Hospital.

19. In the most recent full calendar year (2013), Norton received an estimated \$32 million in federal and state aid payments predicated solely upon increased costs associated with the operation of an accredited pediatric teaching hospital – Kosair Children's Hospital. The federal payments include Medicare graduate medical education payments for direct graduate medical education ("GME") and indirect medical education ("IME") payments. GME payments are intended to reimburse costs teaching hospitals incur in connection with the graduate training of physicians, including the residents' salaries and fringe benefits, the salaries and fringe benefits of faculty who supervise the residents, other direct costs (such as costs of GME clerical personnel) and allocated overhead costs. 42 C.F.R. 413.75 *et seq.* IME payments reflect an add-on payment that is made for each Medicare case to address increases in per-case costs that may

be associated with the patients treated in teaching hospitals. 42 C.F.R. 412.105. Norton received 14,789,488.00 in combined GME and IME aid payments in calendar year 2012.

20. Norton likewise receives analogous state supplemental aid payments under 907 KAR 10:825 §§ 5 and 15(3)(a)(1)(2) – described by the Commonwealth in its State Medicaid Plan as the Intensity Operating Allowance Inpatient Supplement (“IOA”) - premised on its ownership of a pediatric teaching hospital (Kosair Children’s Hospital) operated by the UofL School of Medicine. Norton received \$17,737,917.97 in IOA aid payments in calendar year 2013 for operating Kosair Children’s Hospital.

21. Because the UofL School of Medicine supplies and pays the physicians which lead and staff Kosair Children’s Hospital and incurs the costs of educating students, residents and fellows working there, UofL bears the brunt of education-related expense at Kosair Children’s Hospital. Nevertheless, Norton applies some – but much less than all - of these federal and state aid payments to reimburse itself for amounts it pays UofL as a result of services provided by UofL pediatric residents and faculty serving patients at Kosair Children’s Hospital. For example, in calendar year 2012, Norton reimbursed UofL for some, but not all, of UofL’s cost deficit by paying \$20,909,894 for (i) the salaries and benefits associated with residents assigned to Kosair Children’s Hospital; (ii) faculty and staff support, and (iii) clinical and management services provided by UofL. This left Norton with more than \$11 million in federal and state aid payments in 2012 in excess of its payments to UofL for teaching hospital expenses.

Norton Fails to Perform its Lease Covenants.

22. Norton has systematically failed to perform its Lease covenants and obligations. Norton has failed to operate Kosair Children’s Hospital for the benefit of – or in the interest of – the UofL School of Medicine, and in so doing has failed to provide Kosair Children’s Hospital

funds and resources for pediatric care, service and education benefitting the UofL School of Medicine. Further, Norton has refused to recognize that Kosair Children's Hospital, built on public land owned for the benefit of UofL and contractually tied to the public mission represented by UofL's pediatric teaching programs, is a public asset that is part of a partnership with UofL - rather than private property subject to Norton's exclusive control.

23. Norton has (1) eroded the UofL School of Medicine's ability to use Kosair Children's Hospital to educate students and pediatric residents; (2) reneged on its financial commitments to reimburse the UofL School of Medicine for its increased costs for residents and faculty, education and research required to maintain its accreditation as a pediatric teaching hospital; (3) failed to account for the application of its federal and state aid payments and resources generated by the UofL School of Medicine at Kosair Children's Hospital for UofL's increased costs to the benefit of the UofL School of Medicine and the Kosair Children's Hospital; (4) hid from both UofL and the public information concerning the operations and finances of Kosair Children's Hospital beginning in 2010 by consolidating the Hospital's separate operations into one set of financial statements for the entire Norton "system" - which effectively concealed the revenues, expenses and surplus generated by Kosair Children's Hospital and permitted Norton to use such surplus for the benefit of Norton's other facilities; (5) withheld reimbursement of UofL's increased costs as leverage to negotiate more favorable terms for itself in years of protracted negotiations with UofL over an updated Master Affiliation Agreement (and individual programmatic agreements); and (6) secretly negotiated a Letter of Intent without UofL's knowledge or consent, which purports to delegate joint management and operational control of Kosair Children's Hospital to another university.

Closing access to pediatric specialty service lines.

24. Norton restricted UofL from providing pediatric care, teaching and research at Kosair Children's Hospital by physicians in the pediatric specialties of anesthesiology, radiology and neurosurgery by closing service lines for these specialties. Norton's actions restrict the UofL School of Medicine from doing precisely what is contemplated in a teaching hospital – to care for, educate and teach. UofL cannot recruit and hire physician faculty in specialty service lines which have been closed by Norton.

Diverting pediatric teaching cases from UofL faculty at Kosair Children's Hospital.

25. Norton has degraded UofL's ability to teach residents by establishing and implementing policies to divert pediatric patients – and teaching cases – that would otherwise have been treated at Kosair Children's Hospital by UofL pediatric faculty to Norton's own employed physician network, and at Norton hospitals other than Kosair Children's Hospital.

26. UofL-employed neonatologists direct the nationally-ranked, level four, Neonatal Intensive Care Unit ("NICU") at Kosair Children's Hospital. Nevertheless, Norton has expressly instructed its physician network to refer pediatric perinatal and neonatal patients to Norton-employed physicians and to Norton system hospitals other than Kosair Children's Hospital. Norton has promised physicians in its network that a larger bonus pool will be created for their benefit in exchange for referring perinatal and neonatal patients to Norton-employed physicians rather than UofL physicians. Norton has advised its network physicians that by referring neonatal patients to Norton network physicians, the referring physician can avoid having the patient treated by medical residents and fellows.

27. Norton hired a neonatology practice group in 2011 to take neonatal patients – and teaching cases – from UofL faculty, residents and fellows. Norton has reduced the amounts paid

to UofL's neonatologists for patient care, education and research at Kosair Children's Hospital and allocated these funds to compensate Norton-employed neonatologists.

28. In addition to providing neonatal care in the Louisville area, UofL neonatologists also direct the NICU Nurseries at Owensboro Medical Center in Owensboro, Kentucky and at Western Baptist Hospital in Paducah, Kentucky and provide call coverage at other hospitals in the Louisville metro area. Further, UofL neonatologists provide services at outreach clinics in Western Kentucky.

29. Neonates requiring services higher than those that can be provided in Western Kentucky are referred to Louisville NICUs. A high-level transport service brings neonates to Kosair Children's Hospital from southern Indiana and throughout Kentucky. After hiring its own neonatology group in 2011, Norton began diverting patient referrals from UofL neonatologists at Kosair Children's Hospital by posting labels on telephones installed at hospitals and outreach clinics in Western Kentucky for hiring medical transport to Kosair Children's Hospital NICU (managed by UofL neonatologists) which read "direct access line for neonatal care and transports" and listed a telephone number. Instead of the telephone number going to the Kosair Children's Hospital NICU, however, it is a direct line to Norton-employed neonatologists. Because the number goes directly to the Norton neonatologists, those physicians receive whatever referral is made for a patient being transported to Louisville. Additionally, in instances where the referring physician insists on making the referral to UofL neonatologists, Norton-employed neonatologists solicit the referring physician to refer to Norton-employed neonatologists instead.

30. Norton's practice of hiring competing pediatric practices in specialties such as neonatology and drawing down the number of available teaching cases has caused a decline in

the recruitment and hiring of fellows. For example, UofL was unable to recruit *any* neonatal fellows for the fiscal year beginning July 1, 2011 chiefly as the result of the situation created by Norton's competing neonatal practice sited at Kosair Children's Hospital.

31. Norton's efforts to incent system referrals to its own physicians, and its hiring of a neonatology practice to take patients at Kosair Children's Hospital has reduced the number of Kosair Children's Hospital NICU patients treated by UofL physicians – and teaching cases for residents and fellows - by 25% over the past two years alone. Norton has advised UofL that it has plans that will divert other pediatric patients and teaching cases from Kosair to other sites. Norton's effort to take patients and cases away from UofL faculty, residents and fellows at Kosair Children's Hospital degrades UofL's teaching hospital and makes it more difficult to attract and retain faculty, residents and fellows. These actions by Norton have a negative impact on UofL's ability to meet its ACGME accreditation requirements as it is widely recognized that the number of patients, and thus the variety of types of conditions that residents are exposed to during their medical training, are important to maintaining residency positions and meeting accreditation requirements.

Norton refuses to pay for care, service and education at Kosair Children's Hospital.

32. Beginning as early as 2009, Norton began to renege on funding commitments required under its covenant to "provide pediatric care, service and education benefitting the UofL School of Medicine." The UofL School of Medicine is required to provide a standardized level of medical education to residents and fellows ("MedEd") under ACGME accreditation requirements. Kosair Children's Hospital, Norton and its patients receive direct benefits from the costs paid by UofL's School of Medicine to pay for MedEd costs. The UofL School of Medicine explained to Norton in December 2008 the large and increasing cost deficit that it was

sustaining for MedEd costs and identified Norton's large annual surplus of federal (GME/IME) and state (IOA) payment aid that should be applied to provide patient care, service and education at Kosair Children's Hospital. Based on this discussion and other communications in 2009, Norton agreed with UofL in 2009 that it would use Kosair Children's Hospital resources to reimburse UofL for its shortfall in MedEd costs incurred beginning in 2009 – catching up such accumulated unreimbursed sums as soon as the Master Affiliation Agreement was updated. UofL relied upon that agreement and incurred the costs. The last separate financial statements that Norton issued for Kosair Children's Hospital that were provided to UofL (for the eleven months ended 11-30-09) demonstrated that the Hospital generated more than sufficient funds to meet these commitments, with revenue of \$238 million and a surplus of \$22 million, despite paying the Norton system \$35 million in management fees.

33. UofL's accumulated unreimbursed MedEd costs for fiscal year ("FY") 2009, 2010, 2011, 2012, 2013 and 2014 (through December 31, 2013) were \$807,430, \$812,293, \$894,082, \$971,578, \$1,048,984, and \$543,047, respectively – for a total due from Norton through December 31, 2013 of \$5,077,414.

34. Within several months after Norton made the MedEd commitment, UofL and Norton commenced talks to negotiate a new Master Affiliation Agreement and the individual programmatic affiliation agreements incorporated therein. UofL requested payment of the MedEd deficit amount from Norton. Norton repeatedly affirmed its commitment, but the negotiations continued for months, and months became years.

35. Likewise, in 2010 and 2011, as costs of care continued to increase as a function of increased patient acuity, the UofL School of Medicine was required to increase the number of critical care FTEs. UofL was also required to increase the compensation of existing physicians to

meet the “market” compensation paid to new hires. Before recruiting and hiring critical care physicians to meet that need, UofL asked Norton to negotiate an increased FTE figure under Attachment D to the Critical Care Agreement (Exh. E) in good faith to reimburse UofL for its increased costs. UofL also requested that Norton commit to reimburse UofL for the increased unreimbursed cost that UofL would be required to incur to increase the compensation of existing pediatric faculty to meet the market compensation of new hires. However, while Norton refused to negotiate a new FTE figure for the income guarantee in the Critical Care Agreement at that time as required by the contract, Norton recognized that UofL had to go ahead with the required hiring of critical care physicians and Norton committed to pay for UofL’s increased costs as soon as a new master Affiliation Agreement was negotiated. UofL relied upon this commitment and incurred increased costs for critical care in FY 2011, 2012, 2013 and 2014 (through December 31, 2013) in the amounts of \$273,823, \$989,685, \$465,107, and \$280,881 respectively, for a total of \$2,009,496. UofL has requested payment, but Norton refuses to pay any sum until UofL agrees to terms of a Master Affiliation Agreement acceptable to Norton.

36. Norton agreed in 2012 that it would pay for additional fellows recruited by UofL. UofL hired a forensic fellow in 2012 and 2013 and a pulmonary fellow in 2013. UofL relied upon Norton’s commitment in doing so and has incurred \$200,000 in unfunded costs that have not been reimbursed. UofL has requested payment, but Norton refuses to pay any sum until UofL agrees to terms of a Master Affiliation Agreement acceptable to Norton.

37. Master Affiliation Agreement negotiations between UofL and Norton formally commenced in April 2010, but have continued over a period of almost four years, and have yet to conclude in an agreement with terms satisfactory to Norton. During the negotiations, Norton began to use its mounting unpaid reimbursement commitments to UofL as a bargaining tool. In

2012 and 2013, Norton sought to reduce the amounts already committed to as a condition of agreeing to the terms of a Master Affiliation Agreement and it continues to do so through this day. Norton eventually admitted to UofL that it had used past-due commitments as a bargaining chip in the negotiations, but admitted that this ploy had not worked so far.

38. In addition to specific funding commitments from 2009-present, as part of the Master Affiliation Agreement negotiations, UofL demonstrated the need for increased annual incremental investment in Kosair Children's Hospital and UofL teaching hospital faculty, residents and fellows in order to keep pace with accreditation requirements - and to meet the community's need to maintain Kosair Children's Hospital's competitive position on a national and regional basis. UofL also questioned whether Norton was using Kosair Children's Hospital resources to fund Norton's non-Kosair Children's Hospital expansion projects. Norton agreed in September 2012 to increase its annual support to UofL School of Medicine by \$8,000,000. In reliance upon this commitment, UofL incurred \$9,479,953 in clinical investments and \$4,600,719 in research investments in fiscal years 2012, 2013, and 2014 (through December 31, 2013) for a total of \$14,080,672.

39. Norton has yet to pay UofL either the \$8,008,643 in specific funding commitments for the period 2009-2013 - or the \$14,080,672 incurred by UofL in fiscal years 2012, 2013 and 2014 (through December 31, 2013) in connection with Norton's increased funding commitment of \$8,000,000 per year. Instead, it continues to hold these commitments as leverage in the negotiations for the Master Affiliation Agreement, which have now lasted - in fits and starts - almost four years. As the direct result of Norton's conduct, the UofL Pediatric Department has incurred substantial annual deficits for the past several years, threatening to degrade its teaching mission and ability to attract and retain faculty, residents and fellows.

Norton draws a veil over the operations of a public asset.

40. Additionally, Norton has not fulfilled its obligation under the Lease to permit UofL medical staff or Board of Trustees members to attend Norton Board of Directors and Executive Committee meetings. (*See, e.g.,* Lease, Exh. B at 2 (“NKC will continue the practice of inviting a representative of the U of L School of Medicine staff to its Board of Directors and Executive Committee meetings, to assure *full* and *open* communication between them.”); *id.* at Master Affiliation Agreement at 3 (“Both parties agree to work toward open and regular communication regarding academic programs provided at NHC.”) (Complaint Exh. C).

41. For many years, Norton provided full and open communications, permitting UofL representatives to attend meetings of Norton’s Board of Directors and its Executive Committee, and providing copies of the financial and operating statements of Kosair Children’s Hospital, showing the results of operations independent of Norton’s other system healthcare facilities.

42. However, beginning in 2010, Norton ceased providing financial and operating statements of Kosair Children’s Hospital to UofL and began to exclude UofL representatives from any portion of Norton’s meetings for its Board of Directors and its Executive Committee that addressed non-public information concerning the business of Kosair Children’s Hospital, closing the session of such meetings and preventing UofL representatives from attending.

43. UofL wrote a letter to Norton dated February 14, 2011, notifying Norton that it: “has a contract obligation to permit the University’s designated representatives to attend both the full Board meetings and the Executive Committee meetings under the terms and conditions of the Lease Agreement. The Lease Agreement does not restrict this contract right to “open” sessions of the Board or the Executive Committee.” (Exh. F, February 14, 2011 letter from Ms. Elliott to Mr. Azar at 1.) The letter went on to state that UofL would consider any attempt by

Norton to exclude UofL representatives from any “closed” sessions of the meetings a breach of the Lease.

44. Norton responded that UofL was only permitted to attend certain portions of Norton Board of Directors and Executive Committee meetings, and that Norton could at its discretion “go into Executive Session” and exclude UofL representatives from those portions of the meetings. (Exh. G, February 15, 2011 letter from Mr. Murrell to Ms. Elliott, at 1-2.) By excluding UofL from portions of Board of Directors and Executive Committee meetings at its sole discretion and refusing to provide any financial and operating statements for Kosair Children’s Hospital, Norton is not fulfilling its obligation under the Lease to be transparent with UofL about its operation of Kosair Children’s Hospital.

Norton fails to negotiate and update the Master Affiliation Agreement and programmatic agreements in good faith.

45. Norton has further failed to negotiate in good faith with UofL to amend the existing Master Affiliation Agreement and Critical Care Agreement, as required by the Lease. Both parties agreed in the Lease that the Master Affiliation Agreement would be updated regularly. Because Norton has failed to participate meaningfully in negotiations, the Master Affiliation Agreement, along with many of the programmatic affiliation agreements, have not been amended since 2008. For example, the Critical Care Agreement has not been updated.

46. Norton’s unwillingness to amend the Master Affiliation Agreement is seen in its conduct. For example, Norton abruptly cancelled a long-scheduled meeting between Norton and UofL’s business leaders to discuss the terms and conditions for a new Master Affiliation Agreement in August, only to announce a letter of intent with a *separate* university a few days later.

47. This unilateral act caused UofL to notify Norton that it was in default under the Lease. Rather than negotiating a resolution to the parties' disputes – and before its contractual cure period had concluded - Norton filed this premature suit for declaratory relief – and only then agreed to negotiate the parties' disputes. After lengthy and detailed negotiations over the business terms to be included in a new Master Affiliation Agreement, Norton then inexplicably changed its positions, repeatedly refused to schedule meetings between the parties' business leaders – and after more than two months of such refusals – unilaterally announced that talks were over.

The August 22 Letter of Intent - Norton announces its intention to cede joint control and management of Kosair Children's Hospital to a different university.

48. Norton breached its Lease covenants by announcing its intention to enter into binding agreements with another university via the letter of intent that would (a) delegate joint clinical, operational, and financial control of UofL's pediatric teaching hospital to a *different* university; (b) use Kosair Children's Hospital in a manner that would restrict, diminish, damage, impair, and threaten UofL, and (c) delegate joint recruitment, retention, and placement of pediatric specialists to a *different* university with a *different* teaching hospital. (Complaint Exh. G, at page 2, *infra*.)

49. Norton's repudiation of its obligations under the Lease was magnified because its actions also breached its obligation of transparency under the Lease. Norton did not communicate with UofL in any respect regarding the proposed agreement until *after* it signed the letter of intent with the other university.

CLAIMS FOR RELIEF

Count I-Breach of Contract and the Implied Covenant of Good Faith and Fair Dealing

50. UofL incorporates by reference the foregoing paragraphs of this counterclaim as if fully stated herein.

51. Norton entered into a Lease with UofL as described in paragraph 8 above.

52. Norton and UofL also entered into a Critical Care Agreement as described in paragraphs 15-18 above.

53. Norton has breached the Lease and the Critical Care Agreement, as well as the implied covenant of good faith and fair dealing within each agreement by engaging in the acts and conduct described above, including but not limited to Norton's (1) unilateral and secret negotiation of an agreement to share joint operational control of Kosair Children's Hospital with a different university; (2) refusal to update the Master Affiliation Agreement and programmatic agreements in good faith; (3) failure to provide for care service and education at Kosair Children's Hospital; (4) actions which have eroded UofL's ability to provide pediatric teaching programs at Kosair Children's Hospital; and (5) refusals to reimburse UofL as Norton committed to do for accumulated cost deficits, .

54. Norton's breaches of the Lease and Critical Care Agreement (and their respective implied covenants of good faith and fair dealing) has damaged UofL, and caused UofL to experience significant financial losses, as well as suffer lost teaching, hiring and research opportunities.

55. As a result, UofL is entitled to damages for Norton's multiple breaches of its Lease and Critical Care Agreement with UofL, including monetary damages and any other relief

provided for by the terms of the Lease (including, but not limited to, termination of the Lease) or otherwise warranted by Kentucky law.

Count II-Breach of Fiduciary Duty

56. UofL incorporates by reference the foregoing paragraphs of this counterclaim as if fully stated herein.

57. As partners in providing pediatric care at Kosair Children's Hospital, Norton was in a position of trust and confidence to UofL, and owed UofL certain fiduciary duties, including, but not limited to, a duty to exercise the utmost good faith, loyalty and honesty in the performance of its duties, to avoid taking any improper advantage of UofL, to operate and manage Kosair Children's Hospital for the benefit of and in the interest of the UofL School of Medicine, and to provide full access and information to UofL concerning the operations and finances of Kosair Children's Hospital, a public asset.

58. Norton has breached its fiduciary duties to UofL by engaging in the acts and conduct described above.

59. Norton's breach of its fiduciary duties has damaged UofL. Specifically, UofL has lost significant money, as well as teaching, hiring, and research opportunities.

60. UofL is entitled to a full accounting of the operations and finances of Kosair Children's Hospital and monetary damages sustained as a result of Norton's breach of its fiduciary duties.

Count III-Promissory Estoppel

61. UofL incorporates by reference the foregoing paragraphs of this counterclaim as if fully stated herein.

62. In addition to its contractual obligations in the Lease and Critical Care Agreement, Norton made multiple funding commitments to UofL. (See Paragraphs 32-39, *supra*.)

63. UofL reasonably relied upon Norton's funding commitments and made various expenditures—including salary increases and medical education expenses and clinical and research investments—related to those commitments. UofL had every reason to believe that Norton would honor its commitments.

64. Yet—to UofL's detriment—Norton has failed to fulfill its promise to deliver these funding commitments.

65. Norton's failure to fulfill its promise to deliver funding commitments has damaged UofL and has caused UofL to experience significant financial losses, as well as losing out on teaching, hiring, and research opportunities.

66. As a result, this Court should award UofL monetary damages, which will compensate it for each of the above funding commitments that Norton has not honored.

Count IV-Unjust Enrichment

67. UofL incorporates by reference the foregoing paragraphs of this counterclaim as is fully stated herein.

68. Norton received significant funding from federal and state sources as a result of operating UofL's pediatric teaching hospital.

69. Norton promised to make certain funding payments to UofL.

70. UofL relied upon those commitments and made various expenditures based on those commitments. (See Paragraphs 32-39, *supra*.)

71. Meanwhile, Norton was unjustly benefited by its breaches. In particular, it received the benefits of money provided to Norton from federal and state funding sources as a result of operating UofL's pediatric teaching hospital without providing commensurate funding to UofL and without following through on its funding commitments and other obligations under the Lease and Critical Care Agreement as described above.

72. Accordingly, the interests of equity entitle UofL to restitution for Norton's unjust actions.

Count V-Declaratory Judgment Claim

73. UofL incorporates by reference the foregoing paragraphs of this counterclaim as if fully stated herein.

74. UofL is the beneficial owner of the Property at issue in this case.

75. UofL entered into a Lease with Norton for the Property.

76. Norton has breached the Lease in many respects and has failed to cure these breaches despite timely notice from UofL.

77. Because this action involves an actual controversy between UofL and Norton, UofL is entitled to a declaratory judgment under the Kentucky Declaratory Judgment Act. Specifically, UofL is entitled to a declaratory judgment:

- (a) that the Lease is valid and enforceable against Norton,
- (b) that UofL has authority to enforce the Lease,
- (c) that Norton has breached the Lease and failed to timely cure its breach,
- (d) and that UofL may terminate the Lease, and pursue any other remedies it is entitled to under the Lease.

Request for Relief

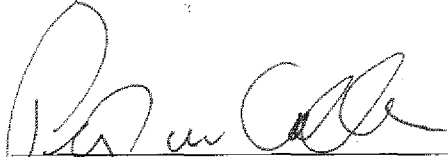
As a result, UofL prays for the following relief:

- (a) Judgment in its favor, including such damages as may be proven;
- (b) Equitable restitution, due to Norton's unjust enrichment;
- (c) A full and accurate accounting for the operations and finances of Kosair

Children's Hospital;

(d) Declaratory judgment that the Lease is valid and enforceable against Norton; that UofL has authority to enforce the Lease; that Norton has breached the Lease and failed to timely cure its breach; and that UofL has the right to terminate the Lease as a result, and pursue any other remedies it is entitled to under the Lease;

- (e) Its attorneys' fees and costs incurred herein; and
- (f) Any other relief to which it is entitled.



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CERTIFICATE OF SERVICE

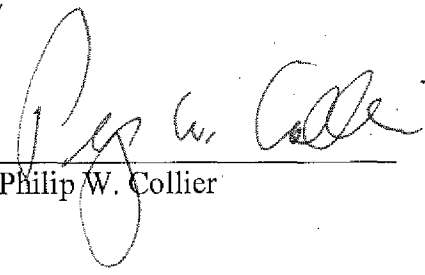
I hereby certify that a copy of the foregoing *Answer and Counterclaim* was served by electronic mail and U.S. Mail, on the 29th of January, 2014 upon:

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