COMMONWEALTH OF KENTUCKY
COURT OF APPEALS
NO. 2013-CA-446

UNIVERSITY MEDICAL CENTER, INC. — APPELLANT

v. — On Appeal From Jefferson Circuit Court
Civil Action No. 08-CI-12392

AMERICAN CIVIL LIBERTIES UNION OF KENTUCKY, INC., ET AL. — APPELLEES

REPLY BRIEF FOR APPELLANT, UNIVERSITY MEDICAL CENTER, INC.

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Certificate of Service

I hereby certify that a copy of this brief was sent by U.S. first-class mail, postage prepaid, this 25th day of October, 2013 to: William E. Sharp, ACLU of Kentucky, Inc., 315 Guthrie Street, Suite 300, Louisville, KY 40202; Jon L. Fleischaker, Jeremy S. Rogers, Dinsmore & Shohl, LLP, 101 S. Fifth Street, 2500 National City Tower, Louisville, KY 40202-2810; Mr. John Keith Smith, 1393 S. 3rd Street, Louisville, KY 40208; and Hon. Angela McCormick Bisig, Jefferson Circuit Court, Division 10, 700 West Jefferson, Louisville, KY 40202. The undersigned certifies that the record on appeal was not withdrawn by the party filing this brief.

Matthew W. Breetz

UMC is not a public agency under Subsection (i) or (j) of KRS 61.870(1). A majority of UMC's governing body (its board of directors) is not appointed by a public agency. Nor was UMC "established, created and controlled" by a public agency.

The Appellees, who implicitly concede that they bear the burden of demonstrating that UMC is a public agency (compare UMC Brief at 14-15 with Media Brief and ACLU Brief), have failed to meet their burden. Although the briefs of the Media Defendants and ACLU contain a variety of misstatements and misleading implications, the Appellees have failed to demonstrate that the trial court erred in making the factual finding that UMC was neither "established" nor "created" by a public agency. Further, they have failed to demonstrate as a matter of fact or law that U of L "established, created, and controls" UMC or that "a majority of" UMC's "governing body is appointed by a public agency." Accordingly, UMC is not a public agency under either subsection (i) or (j).

- "UMC's governing body, its Board of Directors, is appointed by . . . the University of Louisville." (Media Brief, p. 1; ACLU Brief, p. 6.)

Only a minority of the board is *appointed* by U of L's President. The majority of the board (9 to 12 of the 17 total directors) are Community Directors, *nominated* by a Nominating Committee and *elected* by the full board, the majority of whom must be Community Directors. (Bylaws, Exh. 5 to UMC Brief, §§ 4.01, 4.02.) Further, of the 5 to 8 remaining directors, 3 are named in UMC's bylaws by virtue of their office and, accordingly, are not "appointed by" U of L. (*Id.* § 4.02(a).) U of L's President or his designee only appoints 2 to 5 directors on a board that totals 17 members. (*Id.*) Subsection (i), specifically defines "public agency" as an "entity where the majority of its governing body is appointed by a public agency," not, as the Appellees would have it, an entity where a public agency appoints a minority of the governing body.

- The Hospital and its public importance should not be removed from accountability merely because of a "corporate façade." (Media Brief, p. 1, 15.)

The Act should not be rewritten to read as Appellees would have it. The Act applies only to "public records" possessed or retained by "public agencies" as defined by the Act. KRS 61.870(2). The Act does not direct that corporate structures or Kentucky corporation law be ignored or that private entities be deemed public agencies simply because public assets are involved. To the extent that U of L's or other public resources are utilized, records may be obtained from public agencies, but not from private entities.

Further, the Media Defendants have failed to provide any support for their bald assertion that UMC's corporate existence is a "façade." (Media Brief at 1.) Even the Media Defendants admit that UMC was created and organized by two private individuals on behalf of two private companies (Norton and JHHS). (Media Brief at 2.) UMC has maintained its own corporate existence since that time, including maintaining a variety of departments and, as part of managing the hospital, providing staff, performing accounting and recordkeeping functions, handling medical supplies and equipment, managing and maintain the physical space at the Hospital, providing and maintaining technology-related services, and makings its own decisions and developing its own budget. (Taylor Aff., AR 1321, ¶¶ 5-19; Ans. to ACLU Interrog. No. 10, Exh. 3 to Media Brief.)

- UMC was a "corporate shell" and "had no bylaws, and it could not perform its stated corporate purpose" before October 1995, and it adopted its first bylaws on "February 4, 1996." U of L "retains the sole power to amend UMC's Articles of Incorporation and Bylaws." (Media Brief, pp. 3, 23, 25.)

UMC's original bylaws were adopted in **June 1995** and **not February 1996** as the Media Defendants erroneously contend. (UMC Orig. Bylaws, Exh. 1 to UMC S.J. Memo, AR 1045-59; cited at pp. 2-3 of UMC's brief.). These bylaws preceded UMC's competitive proposal, the contract negotiations, and the contract award. The original

bylaws make clear that Norton and JHHS were the founding members of UMC and supplied all of its initial directors. (*See id.* §§ 2.01, 3.02; *see also* UMC Art. of Inc., Exh. A to complaint). The bylaws confirm that the University had no governance or management role when UMC was established and created and when UMC began fulfilling its various purposes set forth in its articles of incorporation.

U of L does *not* retain sole authority to amend the bylaws and articles, the Media Defendants' unsupported assertion to the contrary notwithstanding. The bylaws very specifically provide that the bylaws and the articles of incorporation "may be amended by a vote of a majority of the University Directors and the Community Directors, voting by class . . . ." (Bylaws, Article XV.) Thus, neither the articles nor bylaws can be changed without the agreement of a majority of the Community Directors, who by definition are not trustees, officers, or employees of U of L.

- "Through the [lease and affiliation] agreements" and "numerous other contractual arrangements," the University controls the "details of UMC's operation and management." (Media Brief, pp. 3, 5; ACLU Brief, pp. 3-4, 16-17.)

If U of L controlled UMC as the Appellees claim, then there would be no need for the numerous detailed contractual arrangements between U of L and UMC—U of L would tell UMC what to do and when to do it, and UMC would comply. Because that is emphatically not the way the separate entities operate, they have detailed agreements setting forth every aspect of their relationship. UMC's compliance with the terms of its contracts with U of L (or any other entity) does not mean that U of L (or any other entity with whom UMC has contracts) controls UMC.

Further, the Appellees simply ignore UMC's control of the day-to-day affairs of the Hospital. The contracts between U of L and UMC are consistent with any organization's contractual agreement for management services with another entity—the

requirements and needs of the managed entity are clearly set forth in the parties' contract, while day-to-day operations are left to the managing entity. *See* UMC Brief at 7-8 (setting forth UMC's management of the hospital).

Similarly, the Appellees ignore the fact that the Affiliation Agreement and lease between U of L and UMC are similar to U of L's agreements with Humana—the previous hospital operator and, indisputably, a private entity. *See* Exh. 4 to UMC brief comparing affiliation agreements. Further, the Appellees admit that UMC's Affiliation Agreement was substantially the same when Norton and JHHS were members (when UMC was undisputedly a private entity) and after they withdrew. (Media Brief at 4.) Thus, it is hard to see how that Agreement now makes UMC a public agency.

- UMC was "required to distribute all surplus cash to the University, and UMC could not distribute any such cash to Jewish, Norton, or anyone else." (Media Brief, pp. 4, 13[1]; ACLU Brief, pp. 1, 4, 16.)

Because UMC is a non-profit corporation, it may "make donations for the public welfare or for charitable, scientific or educational purposes," but "no part of [its] income or profit" may be distributed to its members. KRS 273.171(13), KRS 273.161(3), KRS 273.237. Thus, by statute, UMC could not distribute profits to its members, Jewish and Norton. UMC can, however, make donations consistent with its exempt mission, specifically donations to U of L that are "for the public welfare" and for "charitable, scientific or educational purposes." KRS 273.171(13). Indeed, UMC's purposes (similar to the purposes of other non-profit corporations), are to provide care for people who are

[1] Because Kentucky law, without regard to UMC's relationship with U of L, allows UMC to make donations to U of L consistent with its exempt mission, the situation presented here is in no way comparable to the inability of the U of L Foundation to receive "Bucks for Brains" funds available only to postsecondary institutions unless the Foundation was acting "as one and the same" with the University. (Media Brief at 13, citing *University of Louisville Foundation, Inc. v. Cape Publications, Inc.*, 2002-CA-1590, 2003 WL 2274826 (Ky. App. 2003).

in need of medical services, carry on educational activities and scientific research related to care to the sick and injured, promote general health, and "provide, on a nonprofit basis, hospital or health care facilities and services for the care and treatment of persons who are acutely ill . . . ." (UMC Art. of Inc., AR 22, at 1-2.) .

- Through "its request for a new entity to operate" the Hospital, U of L created and established UMC. (Media Brief, pp. 4, 15; ACLU Brief, pp. 1, 13-15.)

If a governmental entity establishes a contest, such as a soap box derby, the governmental entity does not create the winning entrant. Similarly, if a governmental entity issues an RFP to design, build, or collect tolls on a bridge across the Ohio River, the governmental entity does not create the winning bid or winning company. Even if the winning company is a new subsidiary or affiliate of a national company or an entity created by two companies acting together and incorporated specifically for the project, and even if national companies were encouraged by the government to respond to the RFP, the new corporation was neither established nor created by the governmental entity.

Nor does the fact that a contract for the management of a public asset is the object of the RFP alter the equation. For example, Kentucky's marinas are a state asset, yet the private companies managing them on behalf of the Commonwealth are not subject to the open records act as public agencies. Not even the documents they are required to submit to the Commonwealth are open records under the Act. *Marina Management Services, Inc. v. Comm., Cabinet for Tourism*, 906 S.W.2d 318 (Ky. 1995).

The Appellees implicitly concede that the circuit court made a factual finding that UMC was neither "established" nor "created" by U of L. They have not met, and cannot meet their burden to overturn that factual finding. It is only if UMC was "established" *and* created" by U of L that control even becomes an issue, because an entity is a public

agency under Subsection (j) only it was "established, created, *and* controlled" by a public entity. Because U of L did not establish or create UMC, UMC is not a public agency regardless of whether U of L "controls" UMC, which it does not.

- "In the fall of 2007, the University appointed 10 new UMC Directors," at which time "every member" of the board "had been directly appointed by the University." (Media Brief, pp. 5, 7-8, 16-17, ACLU Brief, p. 2.)

The Media Defendants' argument is both irrelevant and erroneous. First, the issue before the Court is whether the majority of the members of UMC's governing body were appointed by a public agency at the time of the open records requests at issue (the summer of 2011). They were not, and the Appellees contentions about the 2007 membership of the governing body are beside the point.

Even if the Media Defendants' contention regarding UMC's 2007 board were otherwise relevant, nothing in the record supports the assertion that U of L appointed ten Community Directors in fall 2007. In ACLU's Interrogatory No. 2, upon which the Media Defendants rely, UMC was asked to identify "every 'Community Director' *elected* to serve on UMC's Board of Directors from January 1, 2007, to the present." (*Id.*) In response, UMC provided a list of directors elected at various times from July 1996 to November 2010, with ten elected members beginning service in October 2007. (Exh. 3 to Media Brief, pp. 2-4.) In response to ACLU's Interrogatory No.3, UMC responded that the Community Directors elected—not appointed—in October 2007 were "[s]eated upon recommendation of Nominating Committee" and most (persons who continued as Community Directors on UMC's board) were "[r]e-elected" at various times "upon recommendation of the Nominating Committee." (*Id.* at 4-5.) Nothing in the record supports the bald assertion that those directors were "directly appointed" by U of L.

- The "slim majority" of Community Directors "is designed to give the false appearance that" U of L doesn't control UMC, and the Nominating Committee will do "exactly what" U of L's President wants because they "are not really independent of U of L." (Media Brief, pp. 6, 8, 10.)

Subsection (i), defines a "public agency" as an "entity where the majority of its governing body is appointed by a public agency." Regardless of the characterization of the majority of Community Directors as "slim," U of L's president or his designees appoints two to five directors on a board that totals seventeen members.

Further the undisputed evidence of record is that the Community Directors, who make up a majority of the board, owe fiduciary duties to UMC and do not act in a representational capacity for U of L. (Community Director Aff., AR 1347-63.) Further, U of L does not control how they vote or act with respect to UMC. (*Id.*) Unsupported and unsupportable assertions to the contrary cannot change reality or the record.

- U of L's President has the "unfettered ability to choose a Nominating Committee that will do exactly what he wants," "can block any potential nomination or appointment" and can "veto" any other proposal if he wants to keep previously elected Community Directors, and can keep incumbent community director nominees by refusing to call for a vote. (Media Brief at 8-9, 17-18.)

In addition to the facts that, as members of UMC's board, U of L's President and each of its board members has a fiduciary duty to UMC (and that the President has never refused to call for a vote), the President cannot block any nominee simply by "say[ing] so." (*Compare* Media Brief at 9 with Bylaws, §§ 6.01(D) and 6.03.) Nor does the President have "veto" power. (*Id.*) Rather, any nominee may be nominated by a "majority" of the Nominating Commission, meaning that 3 of the 4 members must agree, but the 4th (be it U of L's president or another member of the committee) need not agree. Thus, even if the two University Directors agree on a nominee, unless at least one of the Community Director members agrees, that person will not be nominated. Any

Community Director nominee must, in turn, be elected by the full Board. Thus, while University Directors or Community Directors or some combination of Community and University Directors may prevent a Community Director's nomination or appointment, neither U of L's President nor the University Directors acting in unison may cause any person to be nominated or elected without at least some Community Director support at both the Nominating Committee and board levels.

More importantly, Subsection (i) of the Act, defines "public agency" as an entity where a "majority" of the "governing body" is "appointed by" a public agency, not where a public agency plays a part in a nomination and election process (not even if a public agency has the ability to "block" or "veto" nominees). Further, selection of directors by a *nomination* and *election* process does "not fall within the parameters of KRS 61.870(1)(i)." 04-ORD-222.

- Under the current bylaws, "UMC has a 17-member Board of Directors" consisting of "8 University Directors and 9 Community Directors." (Media Brief, p.16.) U of L's President "possesses the authority to appoint and replace" the University Directors, which comprise "nearly half" of UMC's board. (Media Brief, p. 9.)

Under the current bylaws, UMC's 17-member Board must contain a minimum of 4 and a *maximum* of 7 University Directors (plus the University President) and a *minimum* of 9 and maximum of 12 Community Directors. (Bylaws, Exhibit 5 to UMC Brief, § 4.02(a).) Thus, the University Directors can total as much as 8/17 of the total board or as few as 5/17 of the total board.

The President, however, does not have the power to appoint all the University Directors. Rather, UMC's bylaws require that, in addition to the U of L President, the Dean of the Medical School and the Vice President for Health Affairs be 3 of the 5-8 University Directors. (*Id.*) Contrary to the Media Defendants suggested implication, the

naming of *ex officio* members of a governing body in the governing body's bylaws are not the same as appointment of those members. *See, e.g., Fox v. Grayson,* 317 S.W.3d 1, 17 (Ky. 2010); OAG 00-7; OAG 82-565.

Thus, the President has the ability to appoint only 2 to 5 University Directors. *Id.* U of L's President does not appoint a majority of UMC's governing body as required to meet the Subsection (i) definition of "public agency."

- The "power to control who may be considered for appointment constitutes an exercise of the appointment authority." (ACLU Brief at 10, citing *Legislative Research Com'n v. Brown,* 664 S.W.2d 907, 923-24 (Ky. 1984) and *Prater v. Comm.*, 82 S.W.3d 898, 908 (Ky. 2002).

Both cases relied upon by the ACLU concern statutes that were declared unconstitutional under the separation of powers doctrine because the statutes conferred upon another branch of government an executive branch function. In *Brown*, the executive branch function was the power to make appointments; in *Prater* the statute purported to confer upon the judiciary the right to grant parole. Of course, the separation of powers doctrine is not at issue in this case. Moreover, as the Court made clear in *Kentucky Association of Realtors, Inc. v. Musselman,* 817 S.W.2d 213, 214 (Ky. 1991), there is no unconstitutional usurpation of the executive branch's appointment authority where the Governor is not required to appoint anyone from the list, but instead can refuse to make an appointment "until provided with a list that includes a person whom the Governor deems suitable for appointment." 817 S.W.2d at 214.

Even if the separation of powers doctrine were applicable to this issue, and it is not, the Community Directors, just like the Governor in *Musselman*, can refuse to appoint anyone until provided with a Community Director nominee they deem suitable.

- UMC is a public agency because it is like the U of L Foundation. (Media Brief at 12, citing *Cape Publications, supra,* No. 2002-CA-1590; ACLU Brief at 13-14.)

The Appellees ignore the fact that the Foundation was established and created by U of L by resolution of its Board of Trustees. *Courier-Journal & Louisville Times Co. v. Univ. of Louisville Bd. of Trustees*, 596 S.W.2d 374, 375-76 (Ky. App. 1979). In contrast, two private persons on behalf of two private companies created and established UMC, and no U of L representatives, much less U of L officials acting in their "official capacities" or by board resolution, took any action to "establish and create" UMC.

- If a catastrophe eliminates the directors, U of L can "unilaterally appoint the University Directors, who would then be able to appoint all of the Community Directors. (Media Brief at 18.)

Under KRS 273.213, "if a corporation's articles or bylaws, like UMC's, address how vacancies are to be filled, the articles or bylaws control." (UMC Brief at 20-21.) None of the Appellees dispute this fact. Thus, Appellees implicitly concede that, in the event UMC's Board of Directors are somehow lost (yet the catastrophe is not so great that civilization as we know it ends), because UMC's bylaws require nomination by a nominating committee with two Community Directors and election by a board with a majority of Community Directors, UMC will need to seek court guidance regarding how to proceed. *Compare* UMC Brief at 21-22 with Media and ACLU Briefs.

Further, in the event that: (1) all the Community Directors are lost in some manner; (2) UMC does not seek court guidance as to how to proceed as required by KRS 272.213; and (3) U of L appoints board members to replace the Community Directors, thereby appointing the entire board, then at that future and unforeseeable time, and only at that time, UMC might well become a public agency. But that is not the current situation. The Community Directors (a majority of UMC's "governing body") have not been lost and they have been nominated by UMC's Nominating Committee and elected by UMC's board—a majority of UMC's Board has not been "appointed" by U of L.

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