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The insider's guide to investment banking and capital markets

Deal of the Year Awards

HEALTH CARE

BY DANIELLE FUGAZY

Nonprofit? Not Anymore

A hospital chain's transforming purchase shows that 'status change' isn't just for Facebook users

Selling itself to the private-equity giant **Cerberus Capital Management** had the unprecedented effect of turning the **Caritas Christi Health Care** hospital chain from a nonprofit charity to a for-profit business.

The six-location Caritas, now known as **Steward Health Care**, was New England's largest community-based hospital network when it sold itself last year for $895 million.

Like many hospital chains, Caritas was struggling financially. An employer of 13,000 people, it had deferred capital expenditures and was badly in need of improvements. It had a large pension plan that was unfunded, and it needed money to grow.

Dr. **Ralph de la Torre**, Caritas' chief executive, was implementing a turnaround when he contacted **Robert Fraiman**, the CEO of **Cain Brothers & Co.**, to explore options. It quickly became clear that raising capital through the sale of bonds — a common move for hospitals — would not cover the costs associated with all the things Caritas needed to do.

A private capital infusion was starting to look like the best option, but Caritas would have to become a for-profit entity.

Caritas' management team "spent an enormous amount of time with the board exploring alternative options, because they knew how complicated converting to a for-profit hospital system would be," said Fraiman.

"A not-for-profit hospital system had never before gone through a conversion and been sold to a private-equity firm. However, despite the complexities associated with becoming a for-profit hospital system, there were numerous benefits. Caritas Christi would get the capital it needed. It would actually start generating tax revenue for [Massachusetts], which made the state happy, and local jobs would be preserved. And there will probably be an opportunity for corporate staff growth as the company implements its growth plans."

The approval process for Caritas' status change was long and arduous. First, the Massachusetts Public Health Department conducted local hearings for each of the six hospitals, and the state Attorney General's Office, which had to approve the change, had to ensure that the transaction would be in the state's best interest.

Also, the deal required approval not only from the highest court in Massachusetts, but also from the Vatican.

"It was quite extraordinary, and we knew it was going to take a unique and extremely committed private-equity partner to get this deal done," says Fraiman.

Private-equity firms have operated in the health care sector before, but this was a new field for the buyer.

"Cerberus hasn't done any health care deals, so that part was surprising, but they are motivated and deeply knowledgeable about the space," said one dealmaker familiar with the transaction. "And they like controversial transactions and to take on hard deals, so this is a good start for them in the sector." Since the deal was completed, the pension fund has been funded. The hospital chain is paying its debt down, and de la Torre is looking at growth prospects, including opening more hospitals in other states.

"The transaction really has a broader impact, because many hospital systems are in great need of capital, and this transaction certainly opened private-equity firms' eyes, as well as nonprofit hospitals," said the dealmaker familiar with the transaction. "This will definitely lead to other innovative hospital deals in the future." **IDD**

The Deal Teams

Price of deal: $895 million

Adviser to seller: Cain Brothers & Co.

Legal adviser to buyer: Schulte Roth & Zabel

Legal adviser to seller: McDermott Will & Emery