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Health Care Program

Unique Issues in Restructuring Nonprofit Health Care Providers

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Overview: Unique Issues in Restructuring Nonprofit Health Care Providers

Discussion Topics:

- 1 Fiduciary considerations for board members of distressed nonprofit health care providers
- 2 Corporate structures among nonprofit affiliates
- 3 Transaction structures unique to distressed nonprofit health care providers



1 Fiduciary Considerations for Board Members of Distressed Nonprofit Health Care Providers



Fiduciary Duties

FIDUCIARY DUTIES OF DIRECTORS AND OFFICERS OF A NONPROFIT CORPORATION

What are the duties?

- Duty of Care
- Duty of Loyalty
- Duty of Obedience

Directors and Officers must serve the Mission of the NFP Corporation.

- As a practical matter, directors and officers should be sure the corporation's purposes are compatible with their reasons for choosing to serve as a director or officer.
- Corporate Bylaws and Corporate Governance Documents



Duty of Care, Loyalty, and Obedience



Duty of Care

- discharge duties in good faith
- in a manner the director reasonably believes to be in the best interests of the nonprofit corporation
- with the care an ordinarily prudent person in a like position would exercise under similar circumstances



Duty of Loyalty

- duty of undivided loyalty to the nonprofit corporation
- avoid using position or the nonprofit corporation's assets in a way which would result in pecuniary or monetary gain for director or for any member of director's family



Duty of Obedience

- duty to follow the nonprofit corporation's governing documents
- carry out the nonprofit corporation's mission
- assure that funds are used for lawful purposes
- comply with state and federal laws that relate to the nonprofit corporation and the way in which it conducts its activities



Insolvency and Impact on Fiduciary Duties

Directors and officers not required to disregard mission in order to maximize recovery of creditors.

- “[O]nce in bankruptcy, the directors and management owe fiduciary obligations to creditors to ensure that the pursuit of their philanthropic mission is not financed on the backs of creditors without their consent. . . . Nonetheless, the Debtors are not required to abandon their philanthropic mission.” In re W. Va. High Technology Consortium Foundation, 2017 WL 1437067 (N.D. W. Va. April 21, 2017).

The interests of creditors and serving the mission of the NFP must be analyzed and considered in a reasonable way.

- “The best I can discern from the case law is that all of these considerations are supposed to be taken into account and balanced in a reasonable way, and with no other requirement or particular weight to be applied.” In re HHH Choices Health Plan, LLC, 554 B.R. 697 (Bankr. S.D.N.Y. 2016).



How Directors and Officers May Satisfy their Fiduciary Duties in Insolvency

Good Process

- Receive regular reports about the financial health and general operations of the nonprofit
- Develop and implement other necessary reporting
- Review and discuss the financial reports, with these processes documented in the board minutes

Professionals

- Seek outside advice
- Retain professionals
- Better too early than too late

Cash Flow & Strategic Plan

- Immediately assess and manage cash receipts and expenses
- Develop strategy to return to solvency or minimize the negative impact on creditors
- Consider the strategic decisions that need to be explored and enacted
- Consider the timing and level of disclosure to creditors



How Directors and Officers May Satisfy Their Fiduciary Duties in Insolvency (Cont.)

Sale of Assets

- Assess impact on mission and creditors
- Where necessary, implement sale process
- Evaluate bids including impact on mission, creditors and other constituents such as employees

Insider Transactions

- Avoid wherever possible
- Where necessary, obtain information concerning the value of the transaction such as comparability data
- Document the need and basis for approval in advance of the transaction
- Independent Board Members or Committee



2 Corporate Structures Among Nonprofit Affiliates



Sponsor Considerations in Chapter 11 Cases

Sponsors can expect significant involvement in affiliate chapter 11 cases

Key legal and business issues include:

- 1) Corporate Governance
- 2) Management and Operations
- 3) Claims and Litigation
- 4) Contributions and Third-Party Releases



Corporate Governance

- Separate counsel for the sponsor is the best practice
- Bylaws often contain special powers reserved to the sponsor, including authorizing affiliate chapter 11 case filing
- Potential overlap of board members and joint meetings with affiliate board
- Members of the board are typically volunteers
- Fiduciary duties owed to charitable mission
- Officers/management who “wear two hats”



Management & Operations

- Sponsors typically provide “back office” function
- Management agreement governs respective obligations, including structure of cost allocations and “management fee”
- Maintenance of financial controls, affiliate books and records
- Prepare schedules/statements of financial affairs
- Employer of the employees
- Named party on contracts with vendors (but usually not with residents/patients)
- Responsible for tax/regulatory compliance



Claims & Litigation

- Discovery requests targeted at sponsor as custodian of records, much of which is either HIPAA protected or commercially sensitive
- Common interest privilege issues and potential adversity between sponsor and affiliate
- Other stakeholders, such as residents, secured lenders, landlords, and regulatory agencies may look to sponsor to backstop obligations of affiliate



Contributions and Third-Party Releases

- Sponsor DIP Financing to facilitate successful 363 sale/member substitution/plan
- Contributions to consummate court-approved restructuring/wind-down
- Settlement of any claims/releases
- Impact of Supreme Court's ruling in Purdue Pharma on sponsor releases in exchange for contributions and/or settlements
- Post-confirmation litigation/involvement with litigation trustees



3 Transaction Structures Unique to Nonprofit Health Care Providers



Trust Instruction Proceeding

Description	<ul style="list-style-type: none"> State court proceeding that provides a Trustee with judicial consent regarding actions that may be undertaken to modify the terms of the Master Trust Indenture
Opportunities	<ul style="list-style-type: none"> Non-bankruptcy solution (lower implementation costs) Amend principal amortization, interest, term, or discharge outstanding obligations
Considerations	<ul style="list-style-type: none"> Risk of objection or litigation from non-consenting holders Does not address non-bondholder obligations
Example	<ul style="list-style-type: none"> Nonprofit A is underperforming and unable to pay its outstanding debt obligations After considering multiple restructuring options, and with the consent of the Bond Trustee, Nonprofit A elects to pursue an out-of-court sale to a third-party who acquires the assets and assumes all non-bondholder obligations Results of the transaction provided the Bond Trustee with a 70% recovery to par Bond Trustee commences a TIP and upon receipt of court order cancels its outstanding obligations, liens and interests against the borrower

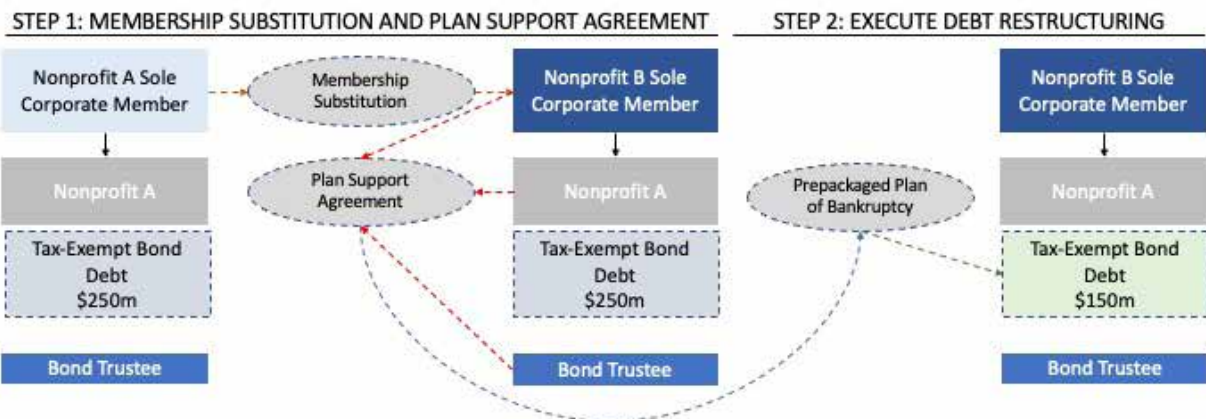


Membership Substitution

Description	<ul style="list-style-type: none"> An acquiring nonprofit entity becomes the new sole corporate member of the target entity, either replacing an existing sole corporate member or converting to a member-managed nonprofit organization
Opportunities	<ul style="list-style-type: none"> Perpetuation of nonprofit mission Potential for expedited regulatory approval process
Considerations	<ul style="list-style-type: none"> Debt restructuring considerations (Donnelly Provision), including preservation of tax-exempt status Timeline to effectuate debt restructuring transaction
Example	<ul style="list-style-type: none"> Nonprofit A is underperforming and unable to pay its outstanding debt obligations After considering multiple restructuring options, and with all required third-party consents (including the Bond Trustee), the Sole Corporate Member of Nonprofit A elects to pursue a membership substitution with Nonprofit B Nonprofit B steps in as the sole corporate member of Nonprofit A Nonprofit B, Nonprofit A, and the Bond Trustee enter into a Plan Support Agreement to refinance the outstanding bond obligations of Nonprofit A through a prepackaged plan of bankruptcy Six months after the membership substitution, Nonprofit A restructures its outstanding obligations



Membership Substitution (Cont'd.)



Faculty

Trinitee G. Green is a shareholder in Polsinelli’s Dallas and Chicago offices, and focuses her practice on complex bankruptcy matters regarding chapter 11 debtors. Although she has represented debtors in a variety of industries, such as manufacturing, distribution, retail, real estate and distressed health care, her expertise is most significant in the health care space. In addition to mega debtors, Ms. Green has represented debtors and creditors in subchapter V cases since the Bankruptcy Code was amended in 2020. In just two years, she co-led two subchapter V cases and helped two small business health care companies confirm plans of reorganization in Delaware and Texas. Ms. Green regularly represents secured and unsecured creditors in restructuring matters. She has represented committees, trustees and receiverships in federal and state courts. She also has experience defending and prosecuting avoidance actions, and she routinely represents secured lenders in contested bankruptcy matters. Ms. Green is a member of ABI, the Honorable John C. Ford, American Inn of Court, the Chicago Foundation for Women and the Young Lawyers Committee of the State Bar of Texas. She is listed in *The Best Lawyers in America* for Bankruptcy and Creditor/Debtor Rights/Insolvency and Reorganization Law for 2025 and named one of its “Ones to Watch.” She received her B.B.A. *summa cum laude* in 2004 from the University of Louisiana Monroe and her J.D. *cum laude* in 2012 from Southern Methodist University.

Nick Harshfield is Chief Financial Officer of Lifespace Communities, Inc. in Dallas. Since June 2020, he has provided oversight and strategic direction for all finance, accounting, IT and development functions. Mr. Harshfield is responsible for developing and implementing strategic plans, integrating technology systems, securing financing for critical development projects, and providing recommendations for acquisitions, divestitures and new business lines at Lifespace. He has more than 30 years of experience in corporate finance and accounting in a wide range of industries, including publicly traded and privately held for-profit and nonprofit companies. Mr. Harshfield’s work spans airlines and manufacturing, and he has more than 21 years of experience in health and human services organizations, including 15 years in senior living. He received his B.B.A. in accounting from the University of Louisville.

Michael W. Morton, CPA is a senior managing director at Ankura Consulting Group, LLC in Dallas. He has over a decade of experience executing corporate finance, restructuring, valuation, M&A and recapitalization assignments, as well as operational restructuring and corporate planning initiatives. Mr. Morton has advised small and large-cap public and private companies, corporate boards, special committees, financial sponsors, lenders and creditor committees in situations involving financial distress. His restructuring advisory experience includes interim management and various leadership roles across financial, operational and strategic situations. Mr. Morton is a member of ABI and the Texas State Board of Public Accountancy, American Institute of Public Accountants and Turnaround Management Association. He received his B.B.A. and his M.S. in accounting from Southern Methodist University Edwin L. Cox School of Business.

Eric E. Walker is a partner with Cooley LLP in its Business Restructuring Group in Chicago, where he focuses his practice on all aspects of financial restructuring, bankruptcy and litigation. He has

represented virtually every major stakeholder in bankruptcy proceedings throughout the country. Mr. Walker has particular experience in restructuring hospital systems, senior-living facilities, continuing-care retirement communities (CCRCs), skilled nursing facilities (SNFs), behavioral health centers and diagnostic medical laboratories. His successful representation of the asset-purchaser in the Health Diagnostic Laboratories (HDL) bankruptcy case was awarded the 2016 Restructuring Deal of the Year (Under \$100M) by The M&A Advisor, and he received an individual Band 5 ranking from *Chambers USA* in 2023. Mr. Walker also has experience in the hotel and hospitality industry and regularly represents hotel owners, developers, operators, lenders and major hotel brands in transactions, state and federal litigation, and bankruptcy. He represented the petitioners before the U.S. Supreme Court in *RadLAX Gateway Hotel LLC, et al. v. Amalgamated Bank* (Case No. 11-166), a landmark chapter 11 bankruptcy case involving secured creditor cramdown. Mr. Walker has been recognized as a leading bankruptcy practitioner by *Chambers USA*, *Lawdragon* and the National Conference of Bankruptcy Judges. He is a member of ABI's inaugural class of 40 Under 40 (2017), and he currently serves on ABI's Board of Directors. He also is an executive editor of the *ABI Journal*, and serves on the advisory board of ABI's Health Care Program. He frequently writes and speaks on issues of bankruptcy and health care law. Mr. Walker received his B.S.B.A. in finance in 2000 from Miami University and his J.D. in 2006 from the University of Connecticut School of Law, where he served on the *Connecticut Law Review*.