

THE COMMONWEALTH OF MASSACHUSETTS
OFFICE OF THE ATTORNEY GENERAL

ONE ASHBURTON PLACE
BOSTON, MASSACHUSETTS 02108

MARTHA COAKLEY
ATTORNEY GENERAL

(617) 727-2200
www.mass.gov/ago

November 25, 2008

Members of the Board of Directors
Holyoke Medical Center, Inc.
c/o Hank J. Porten, President
575 Beech Street
Holyoke, MA 01040

Re: Related Party Transactions/Conflicts of Interest

Dear Directors:

Under its authority to "*enforce the due application of funds given or appropriated to public charities within the commonwealth and prevent breaches of trust in the administration thereof*," (see M.G.L. c. 12, s. 8), the Attorney General's Office, through its Non-Profit Organizations/Public Charities Division (the "Division"), initiated an inquiry regarding certain related party transactions involving Holyoke Medical Center, Inc. (hereinafter, together with its affiliates,¹ collectively, the "Medical Center"). Holyoke Medical Center, Inc., and its affiliates are each Massachusetts public charities and, as such, subject to the Division's enforcement authority.

Specifically the Division has reviewed matters related to transactions whereby the Medical Center procures various lines of insurance coverage through the brokerage services of Goss & McLain Insurance Agency, Inc. ("GMI") (collectively, the "GMI Transactions"). Deborah Buckley, who has been a director of the Medical Center since 2003 and currently serves as its chair, has an ownership interest in GMI. As Ms. Buckley is a director and an officer, the GMI Transactions present a potential conflict of interest and constitute a related party transaction.²

Related party transactions, and the conflicts of interest that are implicit in such relationships, are not, in and of themselves, inappropriate. Nevertheless, because such transactions have the potential for abuse, both the Internal Revenue Service and this Division require disclosure of such relationships in tax and annual report filings (see the Division Form

¹ The Medical Center's affiliates include its parent Valley Health Systems, Inc., as well as MassWEST Services, Inc., Western Mass Physician Associates, Inc., H-C Management Services, Inc., River Valley Counseling Center, Inc., Holyoke Visiting Nurse Association, Inc., and Community Health Foundation of Western Massachusetts, Inc.

² A conflict of interest exists when a person is in a position both to influence an organizational decision and to benefit from that decision. When the decision involves a transaction, it is known as a "related party transaction" because the two contracting parties are "related" through the person having the conflict of interest.



PC, question 24, and the new IRS Form 990, Part IV, questions 25-28 and Schedule L). Consistent with the foregoing, public charities routinely adopt conflict of interest policies that require board members, officers and members of senior management to (i) disclose any relationships which might create a conflict of interest and (ii) provide a process whereby transactions are entered into or renewed with related parties in a manner which assures the best interests of the organization are being served.

We have not evaluated whether the GMI Transactions were, or were not, in the best interests of the Medical Center. Based on our limited inquiry and for the reasons set forth hereinafter, we have, however, concluded that the Medical Center did not comply in all material respects with its long-standing written policies and procedures governing conflicts of interests intended to safeguard the Medical Center's best interests.³ Consistent with that conclusion we have made specific compliance recommendations which the Medical Center has agreed to implement.

Our review of the matters addressed in this letter is limited to a legal assessment of whether the evidence establishes a violation of the Commonwealth's public charities laws. The Division does not express, and nothing in this letter or our findings should be construed to express, any opinion on the business judgments of the Medical Center board or management including, without limitation, contracting or procurement decisions. Except for the reporting obligations set forth hereinafter, this letter concludes our inquiry. Our conclusions and recommendations are based solely on the information submitted to us.

Medical Center Conflict of Interest Policy; GMI Transactions

The Conflict of Interest Policy

The Medical Center has a long-standing Conflict of Interest Policy (the "Policy") set forth both in Article VIII of its bylaws (the "Bylaws") and in a separate undated document, with provisions drawn directly from the Bylaws, entitled "Valley Health Systems, Inc. and Affiliates Policy on Conflict of Interest." The Policy, as it is set forth in Article VIII of the Bylaws:

- (i) defines the components of a "Conflict of Interest" including "Interested Persons" and "Financial Interests" (Sections 1(b), (c) and (d));
- (ii) requires affirmative disclosure (Section 3);
- (iii) requires the governing body, by meeting and vote and without the participation of the Interested Person, to determine whether a Conflict of Interest exists in a disclosed Financial Interest (Section 4);
- (iv) establishes detailed procedures for reviewing and approving a transaction involving a Conflict of Interest including a majority vote by the non-interested

³ While we have not evaluated all aspects of the Policy (as defined above), we note that in general its provisions mandating disclosure, governing body review, and disinterested decision making, are consistent with good governance practice. As such, we have not evaluated compliance with any external good governance standard, practice or guideline but have rather focused our review on the Medical Center's compliance with its own policies and procedures.

- directors that the transaction is in the best interests of the Medical Center, is on fair terms, and that no more advantageous alternative exists (Section 5); and
- (v) requires detailed minutes of the board or committee meeting at which action was taken (Section 6).

The Bylaws also establish a standing Conflict of Interest Committee (the "Committee") and charge it with the responsibility of addressing particular Conflicts of Interest that may arise, and making recommendations to the board of directors regarding such matters. Under the version of the Bylaws adopted in 1997, the Committee was required to meet at least annually to develop and review the Policy; in 2007 that requirement was eliminated and meetings were to be held only upon the request of the board or any member of the Committee for the purpose of making recommendations to the board.

The GMI Transactions

The Division has neither requested nor reviewed the actual insurance policies procured by the Medical Center through the services of GMI, however the Medical Center states that it purchases most (but not all) of its lines of insurance coverage through those services. Additionally, we are informed that the Medical Center has made available to its employees certain lines of personal insurance coverage that employees may elect to purchase; these lines of personal insurance coverage may be procured by employees through the services of GMI.⁴ The Division is also informed that some lines of insurance coverage purchased on its own behalf by the Medical Center, have been purchased without using the brokerage services of GMI.

We have been advised that there is no written agreement between the Medical Center and GMI. We are further advised that the relationship between GMI and the Medical Center dates back to at least the early 1990's. Donald J. McLain, a former director and board chair of the Medical Center, had an ownership interest in GMI during the years prior to 2003 when GMI was providing brokerage services and Mr. McLain was serving as a director.

Evaluation and Conclusions

We have concluded, and the Medical Center has agreed, that: (i) the GMI Transactions constitute a "transaction or arrangement" as described in Sections 1(b), (c), and (d) of the Policy; (ii) Ms. Buckley has a "Financial Interest" in GMI as defined in Section 1(b) of the Policy; (iii) Ms. Buckley is an "Interested Person" as defined in Section 1(c) of the Policy; and (iv) the foregoing constitute a "Conflict of Interest" as defined in Section 1(d) of the Policy.

⁴ The Medical Center, in its recent annual Form PC filings with the Division, disclosed that it made certain payments directly to GMI. These were characterized as "pass-through" premium payments for corporate and employee insurance coverage. The Division is informed that while some of these "pass-through" premiums were used to purchase insurance coverage for the Medical Center itself, the bulk of the amounts were premium payments made by employees for the lines of personal insurance coverage they elected to purchase. It is the understanding of the Division that these premium payments are passed on by GMI to the insurance companies writing the coverage. The Medical Center has agreed to clarify its disclosures with regard to these "pass-through" premium payments in future Form PC filings.

We have also concluded that for each of the years since 2003 in which Ms. Buckley has been a director of the Medical Center, she submitted a disclosure statement setting forth her financial interest in GMI in compliance with the requirements of Section 3 of the Policy. We have, however, further concluded that neither the board nor any committee thereof:

- (i) evaluated, reviewed or discussed Ms. Buckley's disclosure statements, to determine whether a Conflict of Interest existed consistent with the requirements of Section 4 of the Policy; or
- (ii) reviewed, acted on, made findings regarding, or approved the GMI Transactions consistent with the provisions of Section 5 of the Policy.

Moreover, records of the Medical Center suggest that the Committee has met only a handful of times over the last ten to fifteen years, despite provisions in the 1997 version of the Bylaws requiring a meeting of the Committee at least once a year.

This failure to follow policy is not a mere procedural technicality. The GMI Transactions may have been and may still be in the best interests of the Medical Center (as the Medical Center asserts they are); however, by failing to review and act on the disclosed Conflict of Interest in accordance with Sections 4 and 5 of the Policy, the Medical Center has no procedural basis or record upon which to base such a conclusion.

Recommendations

The Medical Center has agreed to take the following steps with respect to the design, content and implementation of its Policy and its future procurement of insurance brokerage services.

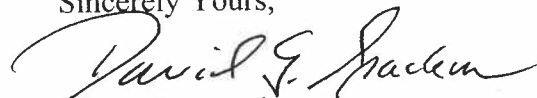
(1) The Medical Center Board of Directors, with the assistance of legal counsel, will undertake a review of (i) the nature, charge, roles, and operations of the Committee and (ii) the Policy, including the form of its disclosure statements, and will make such changes as may be necessary or appropriate to assure that the Committee has the powers and procedures necessary to perform its role and that the Policy provides for a process sufficient to assure that all related party transactions are in the best interests of the Medical Center. Notwithstanding the foregoing, the Division acknowledges that the deficiencies identified by this inquiry were largely related to failure to comply with all aspects of the Policy rather than the substance or provisions of the Policy itself. The review provided herein, and any changes arising from such review, shall be undertaken and completed no later than April 1, 2009 and the Medical Center shall notify the Division upon completion.

(2) The Medical Center Board of Directors, or the Committee, shall review all current disclosure statements to assure that (i) all directors, officers and members of senior management have made current filings and (ii) each disclosed financial interest has been evaluated by the Committee consistent with the Policy. The review provided herein shall be undertaken and completed no later than April 1, 2009 and the Medical Center shall notify the Division upon completion.

(3) The Medical Center, with the assistance of an outside, independent insurance consultant engaged by the Medical Center for such purpose by the Board of Directors, or the Committee, shall, no later than April 1, 2009 have initiated a competitive bidding process, including issuance of a Request for Proposals ("RFP"), for insurance brokerage services for all lines of insurance coverage in which a related party may benefit, directly or indirectly, from the provision of such services. Data acquired from such competitive bidding process will be considered, with the assistance and input of such insurance consultant, by management, the Committee and the Board of Directors consistent with the Policy. The actions provided herein shall be undertaken and completed no later than September 30, 2009 and the Medical Center shall notify the Division upon completion. Please note that nothing contained herein should be interpreted to require, or to suggest that good practice will always require, the engagement of an independent third party when evaluating related party transactions.

Thank you for your cooperation in this inquiry.

Sincerely Yours,

A handwritten signature in black ink, appearing to read "David G. Spackman". The signature is fluid and cursive, with the first name "David" and last name "Spackman" clearly distinguishable.

David G. Spackman

Chief

Non-Profit Organizations/

Public Charities Division

617-963-2110