

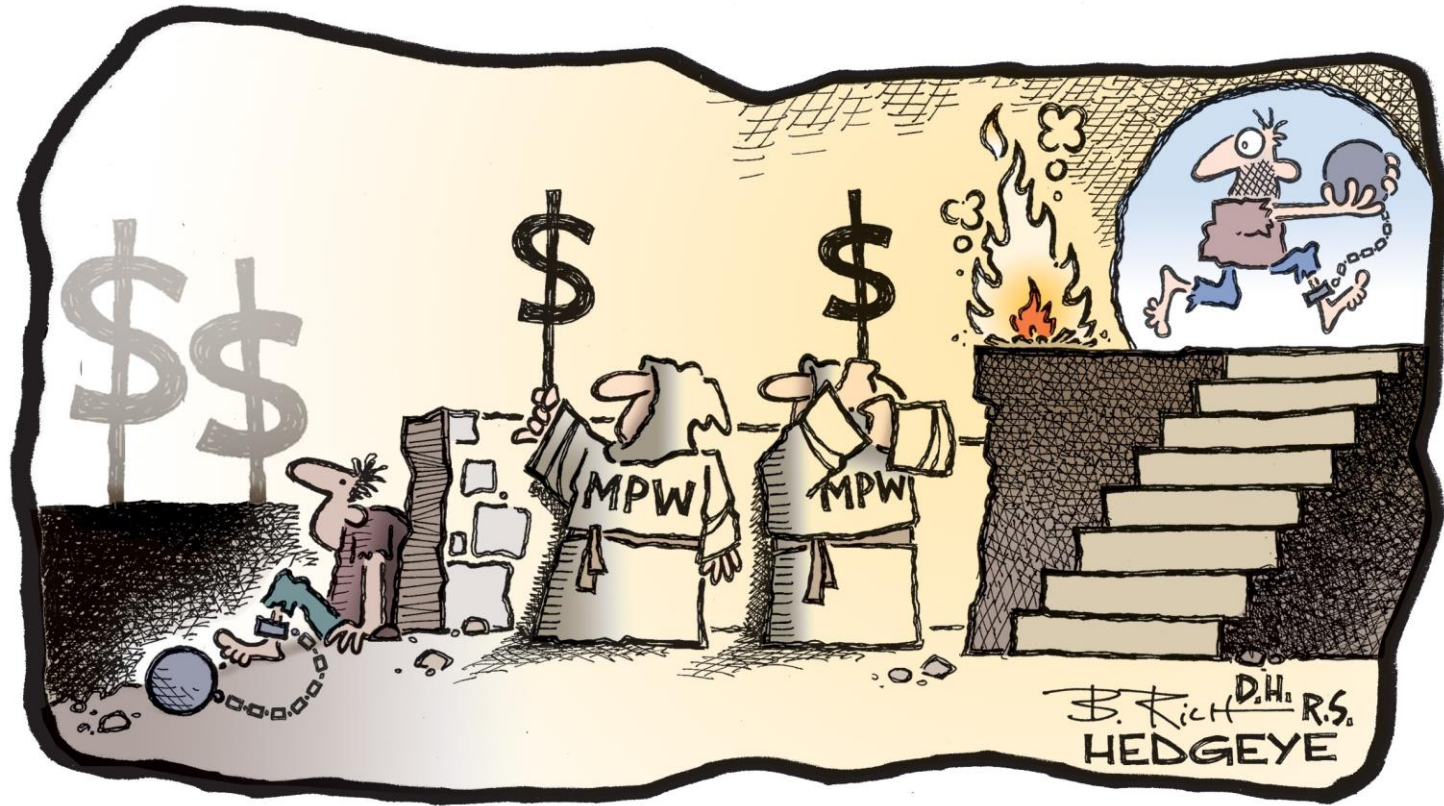
HEDGEYE



# Active **Short** Medical Properties (Dis)Trust (MPW)

Did Prospect Medical Holdings (“Prospect”)  
Pay Any of It’s Rent in 2022? – Part II

October 31, 2023



Medical Properties Trust

HEDGEYE REITs

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# NEW SUBTITLE? THERE, WE FIXED IT...

Our original work and questions on this issue from 9.9.23 can be found [HERE](#) for reference.

HEDGEYE



## Active **Short** Medical Properties (Dis)Trust (MPW)

Did Prospect Medical Holdings (“Prospect”)  
Pay **Any** of It’s Rent in **2022**? – Part II



**[ 1 ] NEW UNPAID 2022 RENT + INTEREST FIGURES?**

# RENT | HEDGEYE OBTAINED THE FULLY-EXECUTED PROSPECT RESTRUCTURING AGREEMENT FROM 5.23.23

This “Agreement” was obtained via a California Public Records Act (“CPRA”) request with the California Department of Managed Health Care (“DMHC”) and is publicly-available. It is among Prospect, PHP Holdings (“PHPH”) and MPW via MPT Picasso Investors TRS, LLC (“Picasso”).

Execution Version

## AMENDED AND RESTATED MASTER RESTRUCTURING AGREEMENT (Vista Investment)

**THIS AMENDED AND RESTATED MASTER RESTRUCTURING AGREEMENT** (this “Agreement”) is made and entered into effective as of this 23<sup>rd</sup> day of May, 2023, by and among **PROSPECT MEDICAL HOLDINGS, INC.**, a Delaware corporation (“Prospect Medical”), **PHP HOLDINGS, LLC**, a Delaware limited liability company (“PHP Holdings”), **PROSPECT HEALTHCARE FACILITIES MANAGEMENT, LLC** f/k/a PHC HoldCo, Inc., a Delaware limited liability company (“ManageCo”), and each of their respective undersigned Affiliates (such Affiliates, together with Prospect Medical, PHP Holdings, and ManageCo, collectively, the “Prospect Parties”) on the one hand, and **MPT PICASSO INVESTORS TRS, LLC**, a Delaware limited liability company (“MPT Picasso TRS”), and its undersigned Affiliates (such Affiliates, together with MPT Picasso TRS, collectively, the “MPT Parties”) on the other hand. The Prospect Parties and the MPT Parties are herein sometimes referred to individually as a “Party” and collectively, as the “Parties”.

**Hedgeye continues to review this document, but for now we wanted to share some new information given its importance. We will continue to update investors as we find additional important/interesting data.**

# RENT | MPW DISCLOSED ONE QUARTER OR LESS OF 2022 UNPAID RENT + INTEREST

MPW stated on page 83 of the 2022 10-K that **until 4Q22, "...Prospect was current on its rent and interest obligations under the various agreements."** The 2022 10-K filing can be found [HERE](#).

Until the 2022 fourth quarter, Prospect was current on its rent and interest obligations under the various agreements. However, with rent and interest now past due and certain of Prospect's restructuring plans yet to be finalized, we recorded an approximate \$280 million impairment charge in the 2022 fourth quarter, as shown in "Real estate and other impairment charges, net" on the consolidated statements of net income. As part of this charge, we reduced the carrying value of the underperforming Pennsylvania properties by approximately \$170 million (to approximately \$250 million) and reserved all non-cash rent for a total of \$112 million. We expect to record rent on our Prospect leases on a cash basis for the foreseeable future. At December 31, 2022, we believe our remaining investment in the Prospect real estate and other assets are fully recoverable, but no assurances can be given that we will not have any further impairments in future periods.



# RENT | HEDGEYE ESTIMATED PROSPECT'S 2022 QUARTERLY CASH RENT + INTEREST AT ~\$33-34 MILLION

- We estimated Prospect's quarterly contractual cash rent + interest owed to MPW at **~\$33-34 million** as of 4Q22.
- This was calculated using available information, including (1) MPW's disclosed gross real estate + loan investments in Prospect, and (2) the stated contractual lease rate/yield of 8.44% for the CA hospitals [HERE](#).
- **Key Point: If Prospect was indeed current until 4Q22, as MPW disclosed in its 2022 10-K, then accrued/recorded but unpaid 2022 cash rent + interest should be less than or equal to this amount, absent any additional information.**
- 10.6.22 press release can be found [HERE](#).
- PA hospital impairment information can be found [HERE](#).
- 2Q23 10-Q filing link [HERE](#).
- 2022 10-K filing link [HERE](#).

(\$ Amounts in 000s)

## Estimated 4Q22 Prospect Cash Rent + Interest

MPW's Investments in Prospect <sup>(1)</sup>	Gross Investment	Lease / Int. Rate <sup>(2)</sup>	Est. Annual Rent / Int.
<b>Description:</b>			
CT Hospital Real Estate <sup>(3)</sup>	457,000	8.12%	37,087
PA Hospital Real Estate <sup>(4)</sup>	421,000	8.12%	34,166
CA Hospital Real Estate <sup>(5)</sup>	513,000	8.12%	41,632
Prospect Term Loan <sup>(6)</sup>	112,900	8.12%	9,162
Foothills Regional, CA Mortgage <sup>(5)</sup>	151,000	8.12%	12,254
<b>Est. Annual Cash Rent + Interest</b>	<b>1,654,900</b>		<b>134,302</b>

( / ) Annualization Factor

4

**Est. 4Q22 Cash Rent + Interest**

**33,575**

### Notes:

- (1) Excludes ~\$50 million convertible loan + ~\$75 million credit facility, which were originated / funded in 2023.
- (2) Estimated using available information. Assumes disclosed ~8.44% lease rate from MPW's 5.23.23 press release was escalated +4%. Lease escalations capped at lesser of +4% or CPI inflation.
- (3) Lease base / gross investment disclosed by MPW in 10.6.22 press release.
- (4) MPW disclosed carrying value of ~\$250 million, following ~\$171 million impairment taken in 4Q22.
- (5) Lease base / gross investment disclosed by MPW in 5.23.23 press release.
- (6) Investment amounts disclosed in MPW's 2Q23 10-Q filing.

# RENT | WHY WAS 2022 AMOUNT NOT QUANTIFIED?

Below is MPW's disclosure on the Prospect restructuring transaction from the 2Q23 10-Q filed [HERE](#) with the SEC on 8.9.23. The below orange highlighted curiously-worded text prompted Hedgeye to explore this issue further.

## Prospect Transaction

In August 2019, we invested in a portfolio of 14 acute care hospitals in three states (California, Pennsylvania, and Connecticut) operated by and master leased to or mortgaged by Prospect Medical Holdings, Inc. ("Prospect") for a combined investment of approximately \$1.5 billion. In addition, we originated a \$112.9 million term loan cross-defaulted to the master lease and mortgage loan agreements and further secured by a parent guaranty. In the 2022 second quarter, we funded an additional \$100 million towards the existing mortgage loan that was secured by a first lien on a California hospital. Prospect's operations were negatively impacted by the coronavirus ("COVID-19") global pandemic commencing in early 2020, but Prospect continued to remain current with respect to contractual rent and interest payments until the fourth quarter of 2022. Accordingly, and due further to the termination of certain refinancing negotiations between Prospect and certain third parties in early 2023, we recorded an approximate \$280 million impairment charge in the 2022 fourth quarter. As part of this charge, we reduced the carrying value of the underperforming Pennsylvania properties by approximately \$170 million (to approximately \$250 million) and reserved all unbilled rent accruals for a total of \$112 million.

However, Prospect continued to pursue a recapitalization plan; and, in late March 2023, Prospect received a binding commitment from several lenders to provide liquidity to pay down certain debt instruments. Along with these commitments from third-party lenders, we agreed to pursue certain transactions with Prospect as part of their recapitalization plan, including originating a \$50 million convertible loan to PHP Holdings, the managed care business of Prospect, in the first quarter of 2023.

On May 23, 2023, Prospect completed its recapitalization plan, which included receiving \$375 million in new financing from several lenders. Along with this new debt capital from third-party lenders, we agreed to the following restructuring of our \$1.7 billion investment in Prospect including: a) maintaining the master lease covering six California hospitals with no changes in rental rates or escalator provisions, and with the expectation that Prospect will begin making cash payments for a substantial portion of the contractual monthly rent due on these California properties starting in September 2023, b) transition the Pennsylvania properties back to Prospect in return for a first lien mortgage on the facilities, c) provide up to \$75 million in a loan secured by a first lien on Prospect's accounts receivable and certain other assets, of which we funded \$25 million on May 23, 2023, d) complete the previously disclosed sale of the Connecticut properties to Yale New Haven ("Yale"), as more fully described in Note 9 to the condensed consolidated financial statements, and e) obtain a non-controlling ownership interest in PHP Holdings of approximately \$654 million, after applying a discount for lack of marketability, consisting of an approximate \$68 million equity investment and \$586 million loan convertible into equity of PHP Holdings (collectively, the "Prospect Transaction"). This non-controlling ownership interest was received in exchange for unpaid rent and interest through December 2022, previously unrecorded rent and interest revenue in 2023 totaling approximately \$68 million, our \$151 million mortgage loan on a California property, our \$112.9 million term loan, and other obligations at the time of such investment.

At June 30, 2023, we believe our remaining investment in the Prospect real estate and other assets are fully recoverable, but no assurances can be given that we will not have any further impairments in future periods.

MPW quantified the unrecorded contractual 2023 rent + interest from Prospect, while on cash accounting...

...but curiously did not quantify already accrued / recorded contractual rent + interest from 2022, right next to it. Why?



# RENT | ADDITIONAL CLAIMS INFO FROM RESTRUCTURING

## PRESS RELEASE

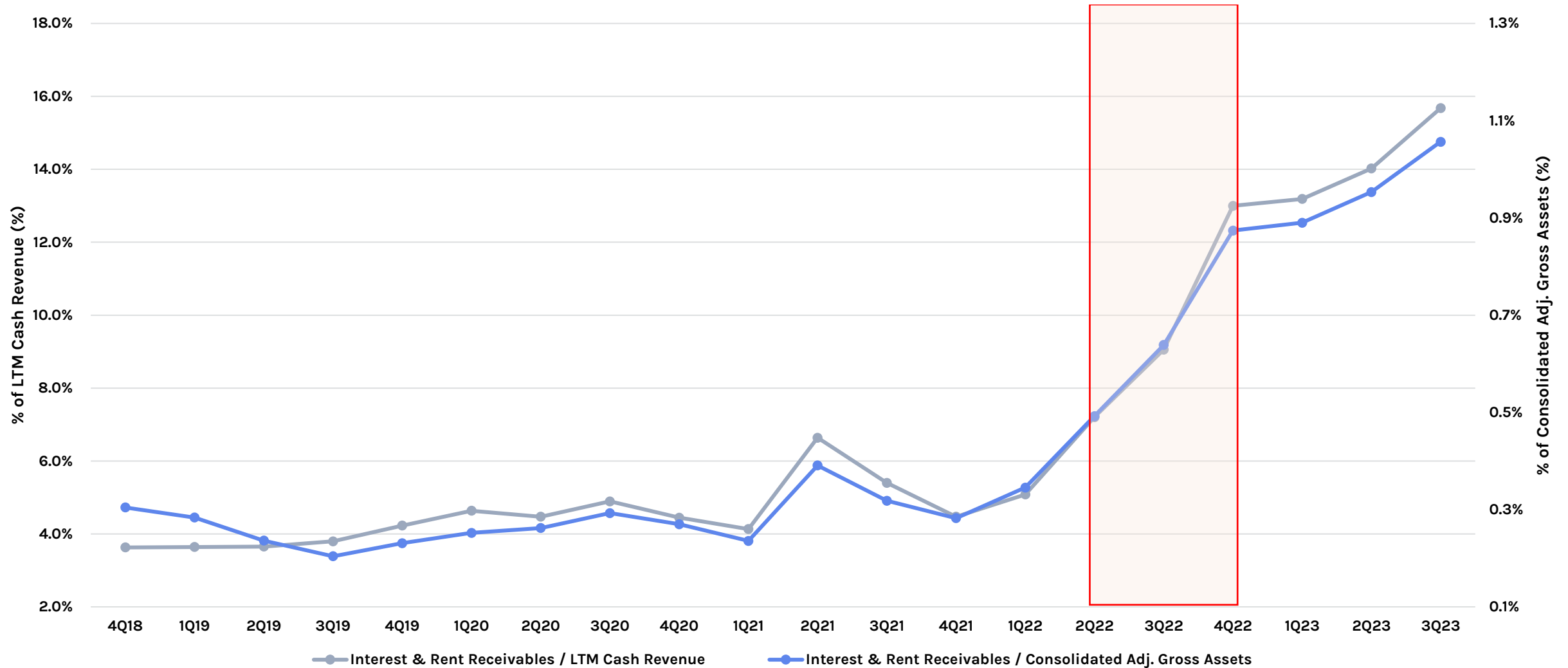
Below is the MPW-stated obligations/claims information from the 5.23.23 “Prospect Recapitalization” press release [HERE](#). This information helped to support Hedgeye’s initial work.

MPT continues to have strong conviction in the embedded value of the Prospect platform and has structured its master leases and security agreements to provide collateral value in addition to its real estate interests, including interests in the equity of Prospect's managed care business. As of the end of the first quarter of 2023, MPT holds \$1.6 billion in total assets related to Prospect that are expected to be reconstituted as follows:

- An approximately \$513 million investment in six leased California hospitals, subject to a master lease scheduled to resume partial rent payments in September and full rent payments at an 8.44% cash yield in March of 2024;
- A \$457 million investment in MPT’s Connecticut real estate which, as previously announced, Yale New Haven Health is expected to acquire in a transaction that is expected to close during 2023’s third quarter. MPT’s investment is expected to be fully recovered through cash proceeds of \$355 million at closing and equity interests in Prospect’s managed care business valued at \$103 million;
- A first lien mortgage loan of \$150 million and equity interests in the managed care business valued at \$100 million, resulting from the transfer to Prospect of Pennsylvania real estate with a book value of \$250 million;
- Loans aggregating approximately \$264 million and accrued rent and interest of approximately \$56 million, along with the previously announced \$50 million convertible loan to the managed care entities are expected to be recovered through equity interests in the managed care business.

# RENT | HEDGEYE SUSPECTED THAT PROSPECT STOPPED PAYING EARLIER THAN 4Q22

We believe something(s) materially negative happened over 2Q-3Q22. MPW's cash A/R accruals began increasing dramatically and >3x'd vs. "normal" levels through to 4Q22. It continued to rise further with 1Q-3Q23 results, indicating separate issues outside Prospect.



# RENT | HEDGEYE ISOLATED FOR UNATTRIBUTED AMOUNTS IN 10-Q DISCLOSURE

(\$ Amounts in 000s)

Prospect Restructuring as Described in 2Q23 10-Q <sup>(1)</sup>

MPW Claims	8.9.23 Amounts	Notes
<b>Description:</b>		
Convertible Loan in PHP - CT Recovery <sup>(1)</sup>	103,000	MPW claimed ~\$355 million cash + equity interest to recover 100% of gross investment at ~\$457 million. At the time MPW guided Yale transaction to close during 3Q23.
Convertible Loan in PHP - PA Recovery <sup>(1)</sup>	100,000	~\$150 million 1L mortgage + PHP equity interest to recover MPW's book value of ~\$250 million. MPW had already recorded a ~\$170 million impairment in 4Q22, implying gross investment of ~\$420 million.
Convertible Loan in PHP - MPW Convertible Loan <sup>(1)</sup>	50,000	~\$50 million convertible loan originated and funded by MPW in 1Q23.
Convertible Loan in PHP - Foothills Mortgage	151,000	~\$151 million mortgage loan on Foothills Regional in CA. MPW upsized the mortgage by ~\$100 million during May 2022. Loan principal cancelled.
Convertible Loan in PHP - Term Loan	112,900	\$112.9 million TL secured by RI hospitals. Loan principal cancelled.
Equity in PHP in Lieu of Cash - Unrecorded 2023 Rent + Interest <sup>(2)</sup>	68,000	MPW explicitly attributed this amount to 2023 previously unrecorded rent + interest. This amount was not previously accrued. Hedgeye believes this amount corresponds to the ~\$68 million (~\$0.11/share) recognized (perhaps inappropriately?) in 2Q23 results. Consists of ~\$55.3 million of rent revenue recorded in "Income from Financing Leases" and ~\$13.5 million of interest income recorded in "Interest and Other Income." Prospect was moved to cash accounting for 2023. This item was non-cash, and the transfer of equity did not/should not have happened.
Unattributed Amount <sup>(3)</sup>	69,100	Did this amount represent 2022 recorded/accrued but unpaid rent + interest and "other obligations?" If so, what were those "other obligations."

Total Implied Consideration from PHP **654,000**

Notes:

- (1) Certain discreet amounts taken from 5.23.23 recapitalization press release.
- (2) This is the ~\$68 million amount recorded/accrued in 2Q23 and highlighted by the WSJ article on 8.18.23.
- (3) This amount represents the delta between the ~\$68 million equity + ~\$586 million convertible loan, and the total PHP equity consideration implied by the 5.23.23 recapitalization press release. MPW did not attribute this amount to a discreet claim in the 2Q23 10-Q.

- MPW disclosed updated Prospect restructuring language in the 2Q23 [10-Q filing](#) on 8.9.23.
- Total consideration increased by ~\$81 million to ~\$654 million vs. amount implied by 5.23.23 release.
- **Controversial ~\$68 million equity interest was recorded in 2Q23, and directly attributed to 2023 previously unrecorded contractual rent + interest.**
- No dollar amount attributed to the recorded 2022 rent + interest. **Why did MPW explicitly disclose 2023 amount, but not 2022 amount?**
- **Approximately ~\$69 million of this new consideration not directly attributed to a specific claim. ~\$69 million was obviously larger than 1 quarter of rent + interest.**
- This was done based on the totality of publicly-available info at the time...

# RENT | THIS IS NEWLY-DISCLOSED DATA ON PROSPECT'S OBLIGATIONS TO MPW AS OF 5.23.23

This Exhibit A can be found on page Exhibit A-1 of the Agreement. These are MPW's actual and stated outstanding obligations totaling ~\$721.6 million. **What is the ~\$182.6 million of "Deferred Amounts?"** That figure is ENORMOUS.

**EXHIBIT A**

**OUTSTANDING OBLIGATIONS**

<b>Phase I Obligations</b>	<b>Amount</b>
Tranche 1 Advance (Foothill Mortgage Loan)	\$ 51,266,700.00
Tranche 2 Advance (Foothill Mortgage Loan)	\$ 100,000,000.00
Tranche 2 Additional Interest (Foothill Mortgage Loan)	\$9,137,500.00
Accrued Base Interest -- Foothill Mortgage	\$6,433,187.69
TRS Note – Principal	\$ 112,937,204.00
Accrued Base Interest – TRS Note	\$4,936,603.11
MPT Advance Convertible Note - Principal	\$50,000,000.00
Accrued Base Interest – MPT Advance Convertible Note	\$588,888.89
<b>Deferred Amounts</b>	<b>\$182,605,385.16</b>
Agreed Pennsylvania Shortfall Amount	\$100,000,000.00
Agreed Connecticut Shortfall Amount	\$102,942,998.00
2020/2021 & 2021/2022 Outstanding Property Insurance Premium	\$783,708.00
<b>TOTAL:</b>	<b>\$721,632,174.85</b>

# RENT | DEFINITION OF “DEFERRED AMOUNTS” PER THE AGREEMENT

Exhibit A of the Agreement – Prospect’s Outstanding Obligations

Section 3.4 on page 8 of the Agreement – the ~\$194 million ties to the sum of the highlighted figures

**EXHIBIT A**

**OUTSTANDING OBLIGATIONS**

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2020/2021 & 2021/2022 Outstanding Property Insurance Premium	\$783,708.00
<b>TOTAL:</b>	<b>\$721,632,174.85</b>

**3.4. Deferred Amounts and Outstanding Property Insurance.** The aggregate outstanding amounts of: (i) the Deferred Base Rent, (ii) the Deferred Interest, (iii) the accrued but unpaid base interest under the Foothill Mortgage Loan Note, and the TRS Note through the date hereof, and (vi) to the extent not included in the foregoing clauses, all Deferred Base Rent and Deferred Interest that may hereafter be deferred as described in the Term Sheet (collectively, the “Deferred Amounts”), are equal to One Hundred Ninety-Three Million Nine Hundred Seventy-Five Thousand One Hundred Seventy-Five Dollars Ninety-Six Cents (\$193,975,175.96). The aggregate amount of Outstanding Property Insurance is Seven Hundred Eight-Three Thousand Seven Hundred Eight and No/100 Dollars (\$783,708.00).



# RENT | "TYING OUT" THE OBLIGATIONS

Very big holes to fill in what was disclosed by MPW, versus what is contained in the Agreement. **What does the MASSIVE ~\$182.6 million represent or tie to?** What was the method used for determining the marketability discount to reach ~\$654 million?

## EXHIBIT A

### OUTSTANDING OBLIGATIONS

Phase I Obligations	Amount
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<b>TOTAL:</b>	<b>\$721,632,174.85</b>

(\$ Amounts in 000s)

Prospect Restructuring as Described in 2Q23 10-Q <sup>(1)</sup>

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Unattributed Amount <sup>(3)</sup>	69,100	Did this amount represent 2022 recorded/acrued but unpaid rent + interest and "other obligations?" If so, what were those "other obligations."
<b>Total Implied Consideration from PHP</b>	<b>654,000</b>	

**Notes:**

- (1) Certain discreet amounts taken from 5.23.23 recapitalization press release.
- (2) This is the ~\$68 million amount recorded/acrued in 2Q23 and highlighted by the WSJ article on 8.18.23.
- (3) This amount represents the delta between the ~\$68 million equity + ~\$586 million convertible loan, and the total PHP equity consideration implied by the 5.23.23 recapitalization press release. MPW did not attribute this amount to a discreet claim in the 2Q23 10-Q.

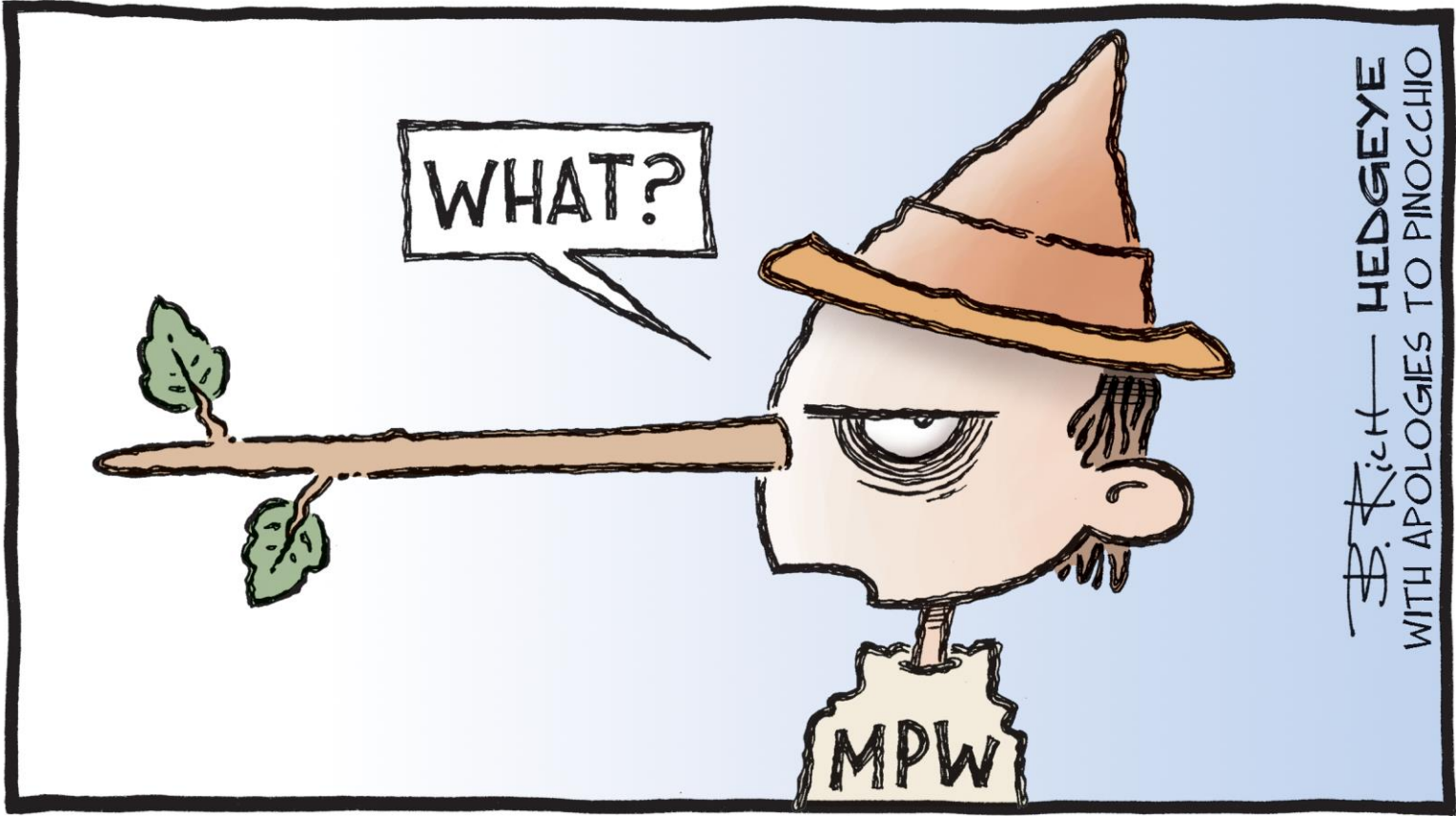
# RENT | HEDGEYE'S INITIAL QUESTIONS FOR MPW MANAGEMENT

There is a massive “hole” to fill here. **~\$182.6 million is an astronomically high amount of deferred/unpaid rent, relative to MPW’s investment in Prospect and Prospect’s annual rent + interest obligations.**

- **What is the ~\$182.6 million of “Deferred Amounts?”** Is that all of the contractually-owed but unpaid rent from Prospect? Does it also include any unpaid interest?
- If so, please explain **how that is consistent with MPW’s 2022 10-K and 2Q23 10-Q disclosure?** Specifically, how is it consistent with the statement that “Prospect was current” on its rent and interest obligations “until the 2022 fourth quarter?”
  - ~\$182.6 million is obviously significantly more than ~\$33-34 million.
  - Hedgeye estimates that ~\$182.6 million represents more than ~1.5 YEARS of unpaid cash rent, when excluding unpaid interest on the Foothill mortgage + TL. ~1.5 years is obviously greater than one quarter.
- What was the exact date that Prospect stopped wiring rent + interest to MPW?
- **Did Prospect pay ANY rent in 2022? A reasonable question given the size of these amounts...**
- How does this factual information, taken directly from the executed Agreement, correspond to MPW’s press release [HERE](#) on the same day (5.23.23)?
- Is the ~\$182.6 million part of the “other obligations” from the 2Q23 10-Q disclosure? If so, why was this not explicitly disclosed, given that it is larger than any other discreet claim?
- What was the methodology for determining the “marketability discount” for the purposes of the 10-Q disclosure?
- Why was this information not disclosed to investors, given that Prospect represented >10% of MPW’s total revenues as of 3Q22?
- **Hedgeye continues to believe that, unless MPW management clearly and transparently addresses these questions, the company remains “un-investible,” especially for fiduciaries. In our view, these issues raise additional questions around management’s transparency and the way it conducts business.**

**[ 2 ] OTHER OBSERVATIONS / QUESTIONS**

- Recall that MPW [changed the AFFO definition](#) throughout 2022. Prospect’s rent was booked as “Interest Income” under a Financing Lease, not as “Rental Revenue.”
- The “Original Restructuring Agreement” was dated as of 7.26.22. This was the same date that MPW curiously amended the Foothill mortgage (we wrote about this [HERE](#) this past weekend) + extended the TL maturity + mentioned the “Managed Care Transaction” for the first time [HERE](#).
  - Based on this newly-available information, clearly these transactions were being discussed earlier than we thought (and disclosed by MPW?).
- As per the final page of the Agreement, there is disclosure around a CT AG investigation that we were not previously aware of:
  3. In April 2023, Prospect Medical Holdings, Inc. (“*PMH*”) and Prospect Medical Systems, LLC (“*PMS*”) received a CID from the State of Connecticut’s Commissioner of Consumer Protection related to an investigation whether hospital funding practices may constitute unfair or deceptive acts or practices in violation of the provisions of the Connecticut Unfair Practices Act. PMH believes that PMS was mistakenly included in the CID because the PMH name was mistakenly listed in the CID as a DBA name for PMS. PMH discussed the purpose and scope of the CID with the Connecticut Attorney General (the “*CT AG*”), and, as requested by PMH during that discussion, the CT AG delivered a letter to counsel for PMH on May 19, 2023, setting forth a revised, limited scope for the CID requests. PMH has begun the process of collecting documentation responsive to the CID requests and has confirmed to the CT AG that the requested information will be delivered to the CT AG on a rolling basis commencing on Monday, May 22, 2023.





For more information, contact us at:

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