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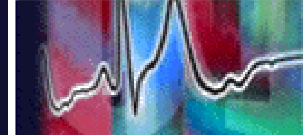
Health Law Pulse



IRS Stepping Up Enforcement of Excess Benefit Transactions

The IRS has announced that it is considering imposing penalties of up to $50,000 on each tax-exempt organization that fails to answer the question on tax Form 990 that asks whether the exempt organization has been involved or became aware of its involvement in an excess benefit transaction within the prior year. An excess benefit transaction is any transaction in which an economic benefit provided by a tax-exempt organization to a disqualified person (i.e., a director, officer, key employee, etc.) exceeds the value of consideration received for the benefit.

Exempt organizations must report excess benefit transactions for the year in which they are discovered, even if the event took place several years before. For those organizations that answer affirmatively, a statement detailing the transaction must be attached to Form 990.

If you have any questions regarding your organization's tax-exempt status or need more information on excess benefit transactions, please contact any member of the Robinson & Cole Health Law Group.

Is Your Laboratory Providing You with Free Services or Supplies in Violation of the Anti-Kickback Statute?

The free provision of employees (i.e., phlebotomists), equipment and supplies to a health care provider by a laboratory may violate the Anti-kickback Statute. This is particularly true where the health care provider's reimbursement includes the cost of laboratory tests and specimen preparation, such as with a composite rate.

This was the opinion of the Office of Inspector General (OIG) issued in Advisory Opinion 04-16 on November 24, 2004. The OIG's position on the provision of free or below-market goods or services to actual or potential referral sources is longstanding and clear. Specifically, such arrangements are suspect and may violate the Anti-kickback Statute, depending on the circumstances.

The OIG referred to its 1994 Special Fraud Alert describing certain laboratory practices that implicate the Anti-kickback Statute. See Special Fraud Alert, "Arrangements for the Provision of Clinical Laboratory Services," 59 Fed. Reg. 65372, 65377 (Dec. 19, 1994). This alert explained that when a laboratory offers or gives an item or service for free, or less than fair market value to a referral source, an inference arises that the item or service is offered to induce the referral of business. Also, with respect to laboratory pricing at dialysis facilities, the Special Fraud Alert identified suspect "swapping" arrangements. Such arrangements involve laboratories offering discounts to a dialysis facility for composite rate tests, payable out of the facility's pocket, in exchange for referrals of all or most of a dialysis facility's noncomposite rate tests, billable by the laboratory directly to Medicare or other federal health care programs.

The OIG found that the arrangement at issue in this advisory opinion has all of the factors that make the provision of such free items or services suspect. First, the receipt of free services and supplies serves as a financial benefit to the dialysis facility because the dialysis facility is otherwise obligated to incur such costs. Hence, the inference arises that the free services and supplies are intended to influence the dialysis facility's selection of a laboratory. Second, the free services and supplies may be viewed as a price reduction or discount on the laboratory's composite rate tests in return for referrals to the laboratory of the noncomposite rate tests, billable directly by the laboratory. As stated by the OIG, "[t]he presence of such a 'discount' arrangement is particularly suspect under the Anti-kickback Statute." As a result, the OIG stated that the proposed arrangement could potentially generate prohibited remuneration under the Anti-kickback Statute.

The Robinson & Cole Health Law Group has experience structuring arrangements with and for laboratories. For assistance, please contact any member of the Health Law Group.

Courts Rule in Favor of Hospitals in Charity Care Litigation

More nonprofit hospital defendants in the charity care class action litigation received good news as courts across the country recently dismissed several lawsuits as legally deficient. These rulings mark a significant turnaround in this litigation and may provide other hospitals with a foothold in mounting legal defenses in similar cases.

Alabama: First Win, First Appeal
The Baptist Health System (BHS), based in Birmingham, Alabama, was the first hospital defendant to obtain a favorable ruling on a motion to dismiss the plaintiffs' charity care claims. Together with the American Hospital Association, BHS argued that the plaintiffs could have raised their excessive billing claims in a related action that those plaintiffs had previously brought in state court against BHS. The Alabama federal court agreed, finding that the plaintiffs' failure to raise those claims in the prior action barred them from suing BHS in a new lawsuit under that theory. The court also dismissed the plaintiffs' claims under the Emergency Medical Treatment and Active Labor Act (EMTALA), finding that those claims were time barred.

The plaintiffs filed an appeal with the U.S. Court of Appeals for the Eleventh Circuit on November 18, 2004. The appeal – the first of its kind – is currently pending.

Victory in Pennsylvania
On November 23, 2004, a federal magistrate judge in the Western District of Pennsylvania recommended the dismissal of the plaintiffs' claims arising under the Internal Revenue Code. In a lawsuit brought against the University of Pittsburgh Medical Center (UPMC), the plaintiffs alleged that the hospital's nonprofit status established a type of implied contract or trust between UPMC and the government. The plaintiffs further alleged that, under this arrangement, the hospital promised to provide uninsured patients with a certain amount of free health care. The magistrate judge rejected this theory and found that Congress did not intend the uninsured to be third-party beneficiaries to the tax-exempt status of nonprofit hospitals. Instead, the Court found that any obligations owed by the nonprofits in exchange for the tax exemption would be enforceable only by the IRS. Based on this reasoning, the judge recommended that the plaintiffs' claims be dismissed because of a lack of standing.

California Dismisses Federal Causes of Action and Remands State Law Claims
One week after the Pennsylvania decision, a federal district court in northern California dismissed all claims brought against Sutter Health by a class of uninsured patients. In the November 30, 2004, decision, the Court explained that the plaintiffs could not pursue any claims arising out of the federal Fair Debt Collection Practices Act (FDCPA) or any implied contract claims relating to Sutter Health's tax-exempt status. With respect to the FDCPA claims, the Court held that the statute generally authorizes lawsuits against debt collectors but only allows claims against creditors under very specific circumstances. Finding that Sutter Health was acting as a creditor in seeking to collect unpaid bills and that none of the statutory exceptions permitting suit against a creditor applied, the

Court dismissed the plaintiffs' FDCPA claims. The Court went on to reject the plaintiffs' implied contract claims applying the same reasoning used by the Pennsylvania decision discussed above.

In a related lawsuit, a separate group of plaintiffs raised various state law causes of action challenging Sutter Health's billing and debt collection practices. Sutter Health successfully removed the case to federal district court on the ground that resolution of the plaintiffs' claims would require the court to resolve substantial federal questions. On January 7, 2005, however, the district court found that the plaintiffs' state law claims presented no federal issues and that no federal jurisdiction existed over the plaintiffs' claims. Accordingly, the judge remanded the case back to California state court for further proceedings.

Michigan Follows Suit
A federal court in Michigan also relied substantially on the same analysis when dismissing all of the plaintiffs' claims against William Beaumont Hospital (WBH). Like the courts in Pennsylvania and California, the Michigan court held that the plaintiffs' implied contract claim failed because they could not demonstrate that the government intended them to be third-party beneficiaries of the nonprofit tax exemption. The court also used the same reasoning adopted by the California court in dismissing the plaintiffs' FDCPA claims. The Michigan court broke new ground, however, when it held that the plaintiffs' EMTALA claims were deficient as pled. Specifically, the court held that the plaintiffs' EMTALA claims failed to the extent that they alleged economic rather than personal harm. The court suggested, nevertheless, that the plaintiffs could avoid dismissal of their EMTALA claims by amending the allegations in their complaint. Finally, the Michigan court rejected the plaintiffs' civil rights claim against WBH on the ground that the plaintiffs failed to demonstrate that the hospital should be treated as a state actor just because it received government funding.

The Robinson & Cole Health Law Group has experience advising hospitals regarding their charity care and tax exemption activities. For assistance, please contact any member of the Health Law Group.

Proposed Pathology Services Joint Venture Ruled Suspect by the OIG
The Office of Inspector General (OIG) issued Advisory Opinion 04-17 indicating that a proposed pathology services joint venture (the Proposed Arrangement) may violate the Anti-kickback Statute.

The Proposed Arrangement involved a company entering into a series of contracts with physician groups to operate pathology laboratories owned by each group at an off-site location. The company furnished all management, supervisory, and administrative services; equipment and space leasing; and, if requested, billing services. In turn, the physician groups paid a flat monthly management fee, a per-specimen fee and, if applicable, a billing and collection fee of five percent of total laboratory revenue.

The OIG has longstanding concerns regarding joint ventures between those in a position to refer (i.e., physicians or physician groups) and those furnishing items or services for which Medicare or Medicaid pays (i.e., a laboratory). Such concerns are particularly prevalent when all or most of the business generated by the joint venture is primarily due to the contractual arrangement between the referring physicians and the existing service provider. The OIG has issued considerable guidance on suspect contractual joint venturesSee e.g., Special Advisory Bulletin, "Contractual Joint Ventures," 68 Fed. Reg. 23148 (April 30, 2003).

The OIG concluded that the Proposed Arrangement at issue in Advisory Opinion 04-17 is suspect. First, the physician groups are expanding into a related line of business that is dependent on referrals from such physician groups. Second, the physician groups are substantially contracting out all operations of the laboratory. Third, the physician groups are committing almost no financial, capital, or human resources to the laboratory and, therefore, are not assuming any real risk. Furthermore, payments by the physician groups vary, based on referrals from the physician groups to the laboratory (i.e., the per-specimen fee). Lastly, the company appears to be paying the physician groups a share of the company profits, based on the physician group laboratory referrals. In other words, the OIG is concerned that the joint venture is simply a vehicle to reward the physician groups for their referrals. Accordingly, the OIG was unable to conclude that the arrangement did not violate the Anti-kickback Statute.

Most significantly, the OIG went further, stating that even if all of the agreements between the parties satisfy a safe harbor to the Anti-kickback Statute, the arrangement would not be protected because of the way the finances were structured (i.e., no risk by the physicians but payment of profits to the physicians based on referrals).

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