

1993-94

NATIONAL HEALTH LAW
MOOT COURT COMPETITION

TRANSCRIPT OF RECORD

Docket No. 92-1958

SUPREME COURT OF THE UNITED STATES

October Term, 1993

ASCLEPIUS HEALTHCARE CORP.,
a not-for-profit corporation, et al.

Petitioners

v.

UNITED STATES OF AMERICA

Respondent

SPONSORS:

Southern Illinois University School of Law

Southern Illinois University School of Medicine,
Department of Medical Humanities

American College of Legal Medicine

UNITED STATES OF AMERICA

Plaintiff

v.

ASCLEPIUS HEALTHCARE CORP.,

a not-for-profit corporation, et al.,

Defendants.

Crim. No. 91-3045

District of Franklin

WEBB, District Judge.

The defendants, Asclepius Healthcare Corporation, a not-for-profit corporation, Ellen Sawyer, its chief executive officer (the "Asclepius defendants") and Drs. Wilber Zuckerman and Fern Arable, (the "physician defendants") were indicted on charges of violating the Medicare and Medicaid Anti-Kickback Statute. 42 U.S.C. 1320a-7b(b). Count I of the indictment alleges that the Asclepius defendants violated the statute by purchasing the physician defendants' medical practice, thereby paying remuneration to induce referrals. Count II of the indictment alleges that the Asclepius defendants paid remuneration to induce referrals under the terms of its subsequent employment contract with the physician defendants. Counts III and IV allege that the physician defendants violated the statute by receiving remuneration to induce referrals pursuant to the same transactions.

This case is now before this court on the Asclepius defendants' motion to dismiss this action under Fed. R. Crim. P 12(b) on the grounds that the Anti-Kickback Statute is unconstitutionally void for vagueness as applied to the facts of this case, as well as on the grounds that the transactions between the Asclepius defendants and the physician defendants do not, as a matter of law, constitute illegal remuneration under the Medicare and Medicaid Anti-Kickback Statute. A separate similar motion by the physician defendants is not currently before the court. This court denies the Asclepius

defendants' motion both on the basis of the vagueness doctrine and on the theory that the financial transactions at issue do not constitute illegal remuneration as a matter of law.

I. FACTS

While there may be some factual disputes between the parties, for the purposes of this motion, the parties have agreed to stipulate to and this court finds the following facts.

Asclepius Healthcare Corp. ("AHC") is a private not-for-profit corporation. It owns and operates Asclepius Medical Center ("Medical Center") a 300-bed acute care general hospital.

The Medical Center is one of two hospitals located in Cape Gonzalez, Franklin, a community with a population of 65,000. The Cape Gonzalez medical community serves a large rural area with a total population of 175,000. The second hospital, St. John Memorial Hospital has approximately 200 beds and a 24 hour emergency room.

Between January, 1989, and October, 1991, there were three family practice medical groups in the Cape Gonzalez community, consisting of twelve family practitioners. During this time, none of these groups was accepting new patients as each was caring for as many patients as it could manage.

Also at this time, the Medical Center provided emergency medical services through its emergency room. If patients were admitted to the hospital, they were assigned an attending physician through an "on-call" schedule. If emergency room patients did not require in-patient medical care, they were treated and instructed to follow up with their family physician. However, if patients had no family physician, they were unable to receive follow up care in a doctor's office because the primary care physicians did not accept new patients. As a result, such patients often returned to the emergency room for routine, non-emergency services such as suture removal, repeat x-rays of healing fractures and cast removal. Further, because it was virtually impossible to get a doctor's office appointment for minor illnesses and injuries, patients turned to the Medical Center's emergency room for these non-emergency services.

Such inappropriate utilization of the Medical Center's emergency room for primary care services increased the cost of the services to patients and overburdened

the physical facility and staffing capacity of the emergency room. Repeated efforts by the three existing private physician groups failed to attract any new family practitioners to Cape Gonzalez during this time.

On April 2, 1991, the Board of Trustees of AHC retained Health Services Consulting, Inc., an independent consulting firm, to make recommendations designed to increase access to primary care in the Cape Gonzalez region. Based upon these recommendations, the Board of Trustees approved a plan to purchase an existing primary care group practice and to recruit additional family practitioners to provide primary and follow-up care. Because it has overturned the "corporate practice" doctrine, Franklin law did not prohibit the purchase.

As part of its plan to increase the number of physicians in Cape Gonzalez, AHC also recruited two new physicians to staff the group practice. Each of the new physicians was offered an employment contract and salary equal to 110% of the net income of Daniel W. Hayes, M.D., the most successful family practice physician currently practicing in Cape Gonzalez.

On August 7, 1991, AHC purchased the assets of Family Practice Associates, P.C., one of the three primary care medical group practices located in Cape Gonzalez, owned by the physician defendants. The terms of this sale are set out in an agreement included as Appendix A to this opinion. Since the sale, AHC has operated this practice at the same location, offering primary care services to patients under the name Asclepius Family Care Clinic ("Family Clinic").

The physician defendants, Drs. Wilber Zuckerman and Fern Arable each also signed a two-year employment contract with AHC at the same salary as the new physicians recruited by AHC to treat patients at the Family Clinic. The terms of these contracts are set out in Appendix B.

Prior to the time of the transaction, Drs. Zuckerman and Arable maintained medical staff privileges at both the Medical Center and St. John Memorial Hospital. At the time, 71% of the patients referred to a hospital for in-patient and out-patient care by the physician defendants were sent to the Medical Center. Currently, 85% of the patients referred to a hospital for in-patient and out-patient care from the Family Clinic are sent to the Medical Center. In its initial year of operation by Asclepius, the Family Clinic generated revenues slightly in excess of operating expenses.

In February 1992, the Office of Inspector General, Department of Health and Human Services initiated an investigation of the transactions and relationship between AHC and the physician defendants. The results were turned over to the Department of Justice and the defendants were indicted.

II. ISSUES

As previously noted for purposes of this motion, the parties have stipulated to the facts as outlined above. The motion presents three basic legal issues for resolution by this court. First, the Asclepius defendants claim that the Medicare and Medicaid Anti-Kickback Statute is unconstitutionally vague as applied to the facts of this case. Second, the Asclepius defendants argue that, as a matter of law, their purchase of the medical group practice does not violate the Medicare and Medicaid Anti-Kickback Statute. Third, they argue that the subsequent employment of the physician-sellers of the medical practice does not violate the statute. Each issue will be discussed in turn.

III. DISCUSSION

Medicare Fraud and Abuse

The Medicare and Medicaid Anti-Kickback statute prohibits health care providers from exchanging patient referrals for any kind of remuneration. 42 U.S.C. § 1320a-7b(b). Providers are precluded from knowingly and willingly offering, paying, soliciting, or receiving bribes, kickbacks, or rebates for items or services that are reimbursable under the Medicare and Medicaid programs. *Id.* Violation of the statute constitutes a felony and subjects providers to fines up to \$25,000 and imprisonment up to five years. *Id.* Upon conviction, a provider must be excluded from payment under the Medicare and Medicaid program. 42 U.S.C. § 1320a-7(b)(7) (administrative proceeding). The statute also authorizes the Office of Inspector General of Health and Human Services to enforce the statute through administrative exclusion proceedings alone. 42 U.S.C. § 1320a-7(b); 42 C.F.R. § 1001.951.

In 1987, Congress directed Health and Human Services to promulgate regulations to establish "safe harbors" which protect certain business arrangements between providers from prosecution. 42 U.S.C. 1320a-7b(b)(3)(E); see 42 C.F.R. § 1001.952. Included among the various safe harbors eventually promulgated were

provisions that protect certain sales of medical practices and bona fide employment relationships. 42 C.F.R. § 1001.952(e), (i).

A. Vagueness Doctrine

The Asclepius defendants argue that the Medicare and Medicaid Anti-Kickback statute is unconstitutionally void for vagueness as applied to the facts of this case. In support of this argument, they claim that the statute does not provide "a person of ordinary intelligence fair notice that his contemplated conduct forbidden", United States v. Harriss, 347 U.S. 612, 617 (1954), and subjects health care providers to the risk of arbitrary enforcement. See Papachristou v. City of Jacksonville, 405 U.S. 156 (1972).

In contrast, the United States argues that the statute is sufficiently definite as applied to the transactions at issue. Although there may be marginal cases in which it is difficult to determine on which side of the line a particular fact situation falls, that is not a sufficient reason to hold a statute's language too ambiguous to define a criminal offense. Miller v. California, 413 U.S. 15 (1973). Further, the government argues that if the general class of offenses to which a statute is directed can be made constitutionally definite by reasonable construction, the court is under a duty to give the statute that construction. United States v. Harriss, 347 U.S. 612 (1954).

After carefully reviewing the cases in this area, this court concludes that the Medicare and Medicaid Anti-Kickback statute provides sufficient notice of the prohibited conduct such that it is not void for vagueness.

B. Remuneration for the Goodwill of a Medical Practice

The United States alleges that the Asclepius defendants have violated the Medicare and Medicaid Anti-Kickback statute by paying more than fair market value for the "hard assets" of the medical practice such as furniture, equipment and supplies thereby unlawfully purchasing the goodwill of the on-going business. The government also cites payment for intangible assets such as the value of the noncompetition clause and the appraised value of the patient lists as remuneration for goodwill. Finally, the government alleges that the amount by which the interest rate paid to the physician-sellers exceeds fair market value constitutes a disguised remuneration for goodwill.

In support of this argument the United States cites United States v. Greber, 760 F.2d 68 (9th Cir. 1985). In Greber, the Third Circuit Court of Appeals held that "if

one purpose of the payment is to induce future referrals, the Medicare statute has been violated even if payments were also intended to compensate the professional services". Greber, 760 F.2d at 72. In addition, they argue that because the transaction does not fall within any of the regulatory safe harbors, it is clearly subject to prosecution.

The Asclepius defendants argue that the purchase of Family Practice Associates, P.C. from Drs. Zuckerman and Arable merely constitutes the lawful purchase of the "hard assets" of a medical practice. They cite the fact that the sale contract (attached hereto as Appendix A) does not recite payment for the goodwill of the practice or for the value of patient referrals. Defendants further argue that the purchase of the practice and consequent increase in primary care physicians in the community has enhanced the quality of care at the Medical Center emergency room and has increased access to out-patient health care. Finally, the defendants claim that the interest rate on the sale encompasses reasonable consideration for not receiving a lump sum payment, and the risk and expense of default by the purchaser.

Alternatively, the defendants argue that even if part of the purchase price were payment for goodwill, such a payment would not constitute illegal remuneration. The defendants point out that payments for goodwill are a common commercial practice in all industries, including the health care industry, and are considered perfectly legal in a free market economy. In addition, the defendants cite United States v. Bay State Ambulance and Rental Service, Inc., 874 F.2d 20 (1st Cir. 1989). In Bay State, the First Circuit held that the government had to "prove that the improper purpose was the *primary* purpose in making a payment". Id. (emphasis added).

Whether payments to providers for the goodwill of a medical practice constitute illegal remuneration under the Anti-Kickback Statute is a question of first impression in this court. However, this court is persuaded that the policy of the Anti-Kickback Statute would be effectively circumvented if hospitals were allowed to induce referrals merely by assigning an artificially high value to the assets of a potential referral source. Therefore, this court denies defendants' motion to dismiss on this theory.

C. Salary and Fringe Benefits under the Employment Contracts

The United States argues that although there is a safe harbor for employees, the provision protects only employment relationships entered into in good faith. Further, the government alleges that the salary term in the contract is in excess of the local market and constitutes remuneration for referrals to the hospital. Finally, they argue

that the physician defendants' participation in the AHC incentive compensation program (nonqualified) under which payments (in addition to salary) are linked to AHC's annual surplus of revenue over expenses constitutes illegal remuneration.

The Asclepius defendants argue that the employment contract falls squarely within the bona fide employment exception to the statute and regulatory safe harbor, and is thus explicitly protected from prosecution. 42 U.S.C. § 1320a-7b(b)(3)(B); 42 C.F.R. § 1001.952. Further, they argue that the salary constitutes the fair market value for board-certified family practitioners. Finally, they point out that the physicians receive incentive compensation payments through the AHC program under the same terms as other key, senior AHC employees including management employees not in a position to refer patients to the Medical Center.

This court finds some merit in defendants' arguments. However, defendants' motion to dismiss on this theory is denied. This court declines to hold as a matter of law that payment of incentive compensation linked to surplus revenues or an inflated salary to a physician does not constitute illegal remuneration.

IV. CONCLUSIONS

Whether in fact knowing and willful kickbacks can be proven is of course another matter. However, this court declines to hold that the transactions at issue do not violate the Anti-Kickback statute as a matter of law.

Therefore, for the foregoing reasons this court denies the Asclepius defendants' motion to dismiss on the grounds that the Anti-Kickback statute is void for vagueness. Further, this court denies the Asclepius defendants' motion to dismiss on the grounds that the transactions between the Asclepius defendants and Drs. Zuckerman and Arable do not, as a matter of law, constitute illegal remuneration under the Medicare and Medicaid Anti-Kickback Statute.

Date: October 15, 1992

/s/
Judge Charlotte Webb

APPENDIX "A"

CONTRACT FOR THE SALE OF MEDICAL PRACTICE

This Agreement is made on August 7, 1991, between Family Practice Associates, P.C., a medical professional corporation, by its officers and shareholders Wilber Zuckerman, M.D. and Fern Arable, M.D. (Sellers) and ASCLEPIUS HEALTHCARE CORPORATION (Buyer).

WHEREAS, Sellers have established a medical practice located at 2500 Shaw Drive, Cape Gonzalez, Franklin, known as Family Practice Associates, and

WHEREAS, Buyer wishes to buy the assets of such practice in order to offer medical services under the name Asclepius Family Care Clinic.

NOW, therefore, Sellers and Buyer agree as follows:

1. Property Sold. Sellers agree to sell Buyer and Buyer agrees to buy the following property of Sellers:
 - (a) the furniture, equipment, medical supplies, fixtures, records, and books located at 2500 Shaw Drive, Cape Gonzalez, Franklin;
 - (b) the accounts receivable;
 - (c) the records of particular patients, if they consent to transferring the records to Buyer;
 - (d) a list of the names and addresses of past and present patients; and
 - (e) Seller's interest in a lease dated October 1, 1988, for the office used by Sellers in their medical practice at 2500 Shaw Drive, Cape Gonzalez.

Sellers warrant that they are the sole owners or lessees of such property and have the full right and power to convey such property to Buyer as herein set forth.

2. Purchase Price. For the purposes of determining the purchase price, the value of the assets listed in Paragraph 1 has been appraised by Medical Appraisers, Inc., at the equal and joint charge of the parties. Pursuant to this appraisal, Buyer agrees to pay Sellers \$306,000.00 for the property listed in Paragraph 1. This price has been allocated as follows:
 - (a) \$250,000 for the furniture, equipment, medical supplies, fixtures, records, and books;
 - (b) \$50,000 for the accounts receivable;
 - (c) \$5,000 for the records of particular patients and the list of names and addresses of past and present patients; and
 - (d) \$1,000 for Seller's interest in the lease for the office used by Sellers in their medical practice.

3. Debts. As part of the considerations for the sale of Seller's medical practice and in addition to the purchase price, Buyer agrees to assume and pay certain debts incurred by Sellers in establishing and operating their medical practice. These debts are as follows:
 - (a) \$15,000 for loan incurred to purchase x-ray equipment; and
 - (b) \$2,000 for loan incurred to purchase lab equipment.

4. Payment of Purchase Price. Buyer shall pay Sellers \$100,000, receipt of which is acknowledged by Sellers, on execution of this agreement. The balance of the purchase price, \$206,000 shall be paid in 48 monthly installments by Buyer.

5. Interest. Buyer shall pay interest to Sellers on the unpaid balance of the purchase price at a rate of twelve per cent.

6. Effective Date of Transfer. The transfer of Seller's medical practice to Buyer shall take effect upon execution of this agreement.

7. Prorations. Sellers and Buyer shall prorate, as of the date of this agreement, the rent payable for leasing the office space, taxes, and the salaries of Seller's employees.

8. Default in Payment. Time is of the essence of this agreement. If Buyer fails to pay Sellers any monthly installment, then Sellers shall retain all monies paid up to that time as liquidated damages for Buyer's breach of the Agreement, Buyer shall forfeit all rights under this Agreement to Seller's medical practice, and this Agreement shall cease to be of any further force and effect.
9. Professional fees. Upon the transfer of Seller's medical practice to Buyer, fees charged for professional medical services shall be set by Buyer.
10. Noncompetition Clause. Sellers agree that they will not engage directly or indirectly in medical practice in Jefferson County, Franklin for four (4) years following the effective date of the transfer of Sellers' medical practice to Buyer or for so long as Buyer shall continue providing family practice services in that county, provided that this provision shall not apply during any period in which Sellers shall be employed by Buyer.
11. Cooperation of Seller. Sellers agree to fully cooperate with Buyer in announcing Buyer's continuation/assumption of Sellers' medical practice to Sellers former and current patients.

This Agreement is executed at Cape Gonzalez, Franklin on the date first above written.

ASCLEPIUS HEALTHCARE CORP.

By: _____ /s/
Ellen Sawyer, Chief Executive Officer

FAMILY PRACTICE ASSOCIATES, P.C.

By: _____ /s/
Wilber Zuckerman, M.D.
President and Individually

By: _____ /s/

Fern Arable, M.D.
Secretary and Individually

APPENDIX "B"

PRIMARY CARE PHYSICIAN AGREEMENT

This Agreement, made and entered into this 7th day of August, 1991, by and between ASCLEPIUS HEALTHCARE CORP. hereinafter referred to as ASCLEPIUS and Wilber Zuckerman hereinafter referred to as DOCTOR.

WHEREAS, ASCLEPIUS is a not-for-profit corporation organized under the laws of the State of Franklin and operates a general, acute care hospital in the City of Cape Gonzalez, Jefferson County, Franklin, and

WHEREAS, ASCLEPIUS also offers primary care medical services to patients in the city of Cape Gonzalez under the name Asclepius Family Care Clinic in a facility located at 2500 Shaw Drive, and

WHEREAS, it is the desire of the parties hereto to enter into an agreement whereby DOCTOR will provide medical professional services on a scheduled basis for the Asclepius Family Care Clinic.

NOW THEREFORE, ASCLEPIUS hereby employs DOCTOR, effective August 7, 1991, and DOCTOR accepts such employment and agrees to provide professional medical services on a regularly scheduled basis, as hereinafter provided.

1. DOCTOR shall be designated as a family practice service physician at Asclepius Family Care Clinic. DOCTOR covenants and agrees that he will assure his fair and equitable share of the duties in the staffing of Family Care Clinic. DOCTOR further agrees that he will provide professional medical services in Asclepius Family Care Clinic so as to diligently, ethically and faithfully insure that the best interests of patients and ASCLEPIUS are served.
2. DOCTOR shall complete an application for appointment to the Medical Staff of Asclepius Medical Center. DOCTOR'S appointment to the Medical Staff and any clinical privileges that may be granted to DOCTOR shall be approved by the Medical Staff Executive Committee and the Board of Directors of ASCLEPIUS. DOCTOR must certify and provide

evidence that he is a medical practitioner and is currently licensed to practice medicine in the State of Franklin. If DOCTOR's clinical privileges are terminated or suspended for any reason, DOCTOR's employment under this agreement shall be terminated at once without further notice.

3. DOCTOR shall, while acting within the scope of his employment with ASCLEPIUS, be covered under its general liability insurance policy.
4. DOCTOR further covenants and agrees that patients will be treated promptly and efficiently, according to the following general policies and procedures:
 - a. DOCTOR may not decline to treat a patient referred to the Family Care Clinic by ASCLEPIUS.
 - b. If DOCTOR determines that a patient requires in-patient hospitalization, DOCTOR may exercise his independent medical judgment in admitting the patient to a medical faculty.
 - c. DOCTOR may provide in-patient medical care or refer a patient to another physician for in-patient care, who shall upon discharge refer such patient for appropriate follow-up care and treatment.
5. ASCLEPIUS covenants and agrees that all decisions of a professional medical nature shall be made by DOCTOR.
6. DOCTOR is expected to work at least eight (8) hours per day and forty (40) hours per week Monday through Friday. Working hours are normally nine to five but may be determined differently from time to time. DOCTOR may also be required to work some nights and weekends in order to accommodate the patients of the Asclepius Family Care Clinic.
7. DOCTOR and ASCLEPIUS agree that remuneration for DOCTOR's services in the Asclepius Family Care Clinic shall be as follows:
 - a. DOCTOR will be paid a salary in the amount of \$17,334 per month to be paid on the first day of each month.

- b. In addition to the salary paid to DOCTOR, DOCTOR shall also be entitled to participate in the Asclepius Incentive Compensation Program pursuant to the terms thereof.
 - c. DOCTOR shall receive the following additional benefits from Asclepius while employed hereunder:
 - i. medical and dental benefits
 - ii. malpractice insurance
 - iii. payment of dues in professional organizations
 - iv. paid vacation of three weeks per year
 - d. ASCLEPIUS shall bill for DOCTOR's time and services. This amount is to be retained by ASCLEPIUS in its entirety.
 - e. DOCTOR shall bill independently for DOCTOR's time and services expended for any in-patient care provided at a hospital.
8. DOCTOR shall not engage in outside gainful employment other than that provided for in this agreement unless such activities are approved by ASCLEPIUS .
9. Upon termination of this agreement for any reason, DOCTOR shall be restricted from directly or indirectly practicing medicine within Jefferson County, Franklin for one year thereafter.

IN WITNESS WHEREOF, parties hereto have affixed their signatures this 7th day of August, 1991.

ASCLEPIUS HEALTHCARE CORP.

By: _____
Ellen Sawyer, Chief Executive Officer

DOCTOR

No. 92-1958

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1992

**ASCLEPIUS HEALTHCARE CORP.,
a not-for-profit corporation, et al.**

Petitioners,

v.

UNITED STATES OF AMERICA,

Respondent.

**On Writ of Certiorari to the United States
Court of Appeals for the Twelfth Circuit**

ORDER GRANTING CERTIORARI

Petition for Certiorari is hereby granted on the following issues:

1. Whether the Medicare and Medicaid Anti-Kickback statute is unconstitutionally vague as applied to the facts of this case.
2. Whether, as a matter of law, payments to physicians for the goodwill of an on-going business in the purchase of a medical practice may constitute illegal remuneration under the Medicare and Medicaid Anti-Kickback statute?
3. Whether, as a matter of law, a physician's salary and fringe benefits under an employment contract may constitute illegal remuneration under the Medicare and Medicaid Anti-Kickback statute?

IT IS SO ORDERED,

Date: June 15, 1993