

More Muscle For Medicare In Health Care Bankruptcies

By Dawn Messick and Judith Waltz

For many health care entities, Medicare payments constitute a large percentage of their dependable revenue. Distressed health care entities often have incurred Medicare overpayments, and also often count on continued Medicare revenues to help keep them afloat after a bankruptcy filing. Entities which seek liquidation hope that they can resolve the Medicare claims along with the rest of their debts in the bankruptcy court. Consequently, “what will Medicare do?” with respect to its overpayment claim is a frequent topic of concern in health care bankruptcies.

Medicare regulations define the term “provider” (mostly paid under Medicare Part A) distinctly from “supplier” (mostly paid under Medicare Part B)[1], and most reported decisions which involve approval for post-petition recovery of prepetition Medicare debts have involved providers and theories of recoupment available under Medicare Part A (specifically, 42 U.S.C. § 1395g(a)) for entities seeking to reorganize under Chapter 11.[2] Although the Medicare regulations that address recoupment and offset do not distinguish between Parts A and B, section 1395g(a), the statutory basis for allowing recoupment in earlier decisions, is applicable only to providers.[3]

Medicare reimbursement methodologies and participation obligations differ for providers and suppliers. For example, a physician who falls within the definition of “supplier” can basically terminate Medicare participation at will; in contrast, however, a “provider” must first advise the Centers for Medicare and Medicaid Services of a proposed termination date, await CMS approval and provide adequate notice to the public.[4] Even the regulatory basis for successor liability when there is a change of ownership is technically only applicable to providers, however, CMS applies successor liability to some suppliers as well.[5]

Aside from physicians, the entanglement of Medicare and some Part B suppliers (such as suppliers of durable medical equipment and ambulance companies) is increasing, with additional obligations inclusive of competitive bidding contracts and site inspections by Medicare contractors as part of the enrollment process, which, in turn, may lessen the operational distinctions between providers and suppliers.

Despite the historical differences between Medicare Parts A and B, a recent case supports

and expands Medicare's authority for collecting prepetition Medicare overpayments by allowing Medicare to recoup its debts by withholding post-petition reimbursements owed to a physician supplier (Medicare Part B) who had filed for an individual bankruptcy under Chapter 7.[6] The United States District Court for the District of South Carolina affirmed the ruling of the United States Bankruptcy Court for the District of South Carolina that such withholding is allowed under the doctrine of recoupment and, therefore, does not violate the discharge injunction in a Chapter 7 bankruptcy case.

The facts of the case are simple. Years prior to filing for Chapter 7 bankruptcy, Dr. Gary Fischbach entered into a Medicare Participating Physician/Supplier Agreement, which allowed Fischbach to become a participating supplier for Medicare. The Centers for Medicare and Medicaid Services and Palmetto Government Benefits Administrators LLC, as the Medicare contractor (together, the "appellees"), prepetition, informed Fischbach that the Medicare program had overpaid Fischbach.

Fischbach unsuccessfully appealed through the administrative process. He was notified by the Medicare contractor that his subsequent claims had not been sufficient for recovery of the overpayment, and by March 2010 the overpayment had increased (presumably due to the addition of interest) to the approximate amount of \$410,000. Fischbach filed for bankruptcy under Chapter 7 in April 2010.

Fischbach continued to provide physician services to Medicare beneficiaries post-petition and post-discharge; however, appellees, during this time, withheld Medicare payments owed to Fischbach in order to collect on the overpayments made for services performed prior to the bankruptcy filing. Fischbach commenced an adversary proceeding in the Bankruptcy Court asserting, in part, that such withholding by the appellees violated the Chapter 7 discharge injunction.

The primary issue on appeal, as in various prior cases involving Medicare overpayments collected post-petition, was whether Medicare's withholding of post-petition payments owed to Fischbach was a set-off of the prepetition overpayments made by Medicare or whether such withholding was a recoupment of the prepetition overpayments made by Medicare.

The court explained the standards and applicability of set-off and recoupment. The court further noted that in order for doctrine of recoupment to be applicable: (1) there must be an

overpayment; and (2) “both the creditor’s claim and the amount owed to the debtor must arise from a single contract or transaction.” In other words, for recoupment to apply in the Fischbach case, the prepetition overpayments made to Fischbach and the post-petition amounts withheld by appellees must arise from a single contract or transaction.

On appeal, not surprisingly, Fischbach argued that the amount overpaid by Medicare prepetition, and amounts withheld post-petition, should be considered under the doctrine of set-off — if so, such prepetition debts would be discharged. The court noted, however, that in finding that the Chapter 7 discharge injunction was not violated by the withholding of the appellees, the Bankruptcy Court applied the recoupment doctrine and found that the Medicare prepetition overpayments made to Fischbach and the post-petition recoupment of such overpayments “occurred under a single contract and constituted a single transaction.”

The court then detailed the split among the Third Circuit, on the one hand, and the First, Ninth and District of Columbia Circuit Courts of Appeals, on the other hand, and the key cases from these circuits as to whether withholding post-petition reimbursement payments in order to collect, or recoup, prepetition overpayments is considered a recoupment or a set-off.

The Third Circuit Court of Appeals held in *Univ. Med. Ctr. v. Sullivan*, 973 F.2d 1065, 1079 (3d Cir. 1992), as stated by the court, that withholding post-petition reimbursements to collect overpayments from prior years was an “improper set off” as opposed to an allowed recoupment.

Contrary to the holding of *University Medical Center*, courts within the First, the Ninth and the District of Columbia Circuit Courts of Appeals have held that withholding post-petition payments to collect overpayments made prepetition is part of a single transaction and, consequently, have been considered an allowed recoupment. See *In re TLC Hospitals Inc.*, 224 F. 3d 1008 (9th Cir. 2000); see also *United States v. Consumer Health Services of Am. Inc.*, 108 F.3d 390, 395, 323 U.S. App. D.C. 336 (D.C. Cir. 1997); *In re Holyoke Nursing Home Inc.*, 372 F.3d 1 (1st Cir. 2004).

The court noted that, as acknowledged by the bankruptcy judge in the within case, the Fourth Circuit is also split on the specific issue of whether withholding post-petition reimbursement payments in order to collect prepetition overpayments is considered a recoupment or a set-off.

The court concluded that it “agrees with the majority view and the Bankruptcy Court’s decision below that recoupment of prepetition Medicare overpayments by withholding post-petition Medicare reimbursement payments does not violate the discharge injunction.” Further, the court reasoned that equitable considerations and public policy support the Bankruptcy Judge’s decision.

As to equitable considerations, the court noted that it would be inequitable to permit Fischbach to accrue Medicare overpaid reimbursements prepetition and, then, still continue to receive Medicare reimbursements for post-petition claims; and, that being allowed to do so would result in Fischbach receiving a windfall. Also, public policy was explained to be supported by the decision in that appellees can use any recouped funds to provide to other Medicare providers as reimbursements.

The majority view, as relied upon by the court in *In re TLC Hospitals Inc., United States v. Consumer Health Services of Am. Inc.*, and *In re Holyoke Nursing Home Inc.*, endorses the theory that the withholding of payments post-petition to collect overpayments made prepetition is allowed as a recoupment and is part of a single transaction. All three cases, however, involve non-individual Chapter 11 debtors who were institutional providers under Part A of the Medicare program (such as a hospital or skilled nursing facility), as opposed to Fischbach — an individual Chapter 7 debtor who was a Part B physician supplier under the Medicare program.

Further, despite Fischbach’s arguments to the contrary, the court found that the distinction between “providers” and “suppliers” is “not relevant to the issue of reimbursement for over and underpayments.” The court found an integrated transaction giving rise to recoupment even without the executory contract framework which a Part A provider agreement has provided in most previously reported cases.[7]

In the prior cases, accepting the Medicare provider agreement as an executory contract emphasized the ongoing integrated relationship between CMS and the provider, and provided support for the idea that a provider/debtor could not “pick and choose” which obligations of the provider agreement it would assume — indeed, recoupment of overpayments being one of those obligations of the provider agreement.

The Fischbach case, therefore, supports and expands Medicare's ability to recoup prepetition overpayments into the individual Chapter 7 arena and against Part B suppliers.

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[1] See 42 C.F.R. § 400.202.

[2] Title XVIII of the Social Security Act, Part A (Medicare Hospital Insurance Benefits) states, in part:

The Secretary shall periodically determine the amount which should be paid under this part to each provider of services with respect to the services furnished by it, and the provider of services shall be paid, at such time or times as the Secretary believes appropriate (but not less often than monthly) and prior to audit or settlement by the General Accounting Office, from the Federal Hospital Insurance Trust Fund, the amounts so determined, with necessary adjustments on account of previously made overpayments or underpayments; except that no such payments shall be made to any provider unless it has furnished such information as the Secretary may request in order to determine the amounts due such provider under this part for the period with respect to which the amounts are being paid or any prior period.

See Soc. Sec. Act § 1815(a) [42 U.S.C. § 1395g(a)].

[3] See 42 C.F.R. § 405.371.

[4] See 42 C.F.R. § 489.52.

[5] See 42 C.F.R. § 489.18.

[6] *Fischbach v. Centers for Medicare and Medicaid Services*, 2013 U.S. Dist. LEXIS 39855 (March 22, 2013)

[7] The Schedules of Assets and Liabilities filed on April 22, 2010 in the bankruptcy case sets forth that the debtor, Fischbach, had no executory contracts