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Binding the Government in Health Care Restructurings: What Notice Is Required?

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A recent decision from a Texas bankruptcy court provides an important roadmap for health care debtors seeking to bind the Centers for Medicare and Medicaid Services (CMS) to confirmed chapter 11 plans. CMS is the federal agency that administers the Medicare program and, in cooperation with the various states, the Medicaid program.

In *La Fuente Home Health Services Inc., v. Burwell (In re La Fuente Home Health Services Inc.)*, [1] the bankruptcy court made two noteworthy rulings. First, the court determined that it had subject-matter jurisdiction to enforce provisions of a plan preventing CMS from exercising recoupment rights, regardless of whether the court had jurisdiction to modify the claim in the first place. Second, it denied summary judgment to the agency, which argued that the debtor could not obtain injunctive relief enforcing the plan because there was insufficient evidence regarding service of process prior to plan confirmation.

In so ruling, the court side-stepped a jurisdictional imbroglio over whether 42 U.S.C. § 405 requires the exhaustion of administrative remedies before a bankruptcy court can exercise jurisdiction over disputes involving Medicare. [2] While this jurisdictional issue remains unresolved, the lesson for prudent practitioners is clear: Not only should health care debtors serve CMS directly with notice of a bankruptcy petition, but any plan that could conceivably alter CMS's rights and remedies should be served on the agency prior to a confirmation hearing.

Facts and Procedural Background

The basic dispute in *La Fuente Home Health Services* centered on whether a confirmed plan and § 1141 of the Bankruptcy Code prevented CMS from exercising recoupment rights based on an unpaid prepetition Medicare overbilling claim — and whether a debtor could obtain post-confirmation injunctive relief against the agency to bar agency recoupment efforts. [3] The issue arose in the context of an adversary proceeding brought by the debtor against CMS and Palmetto GBC LLC, a Medicare Accountability Contractor (MAC) [4] and agent of CMS.

By way of background, the debtor filed a bankruptcy petition in May 2014 and scheduled an unsecured (but disputed) claim in favor of Palmetto in the approximate amount of $720,000. The debtor described the basis of the claim as "[c]ollecting for Medicare[.]" [5] While the debtor listed Palmetto on its matrix of creditors and provided Palmetto with notice of the bankruptcy filing, the debtor did not separately schedule a claim in favor of CMS, list CMS on its matrix of creditors, or directly provide CMS notice of the filing. [6] Neither Palmetto nor CMS entered an appearance in the case. [7]

The debtor subsequently filed a disclosure statement and plan proposing to reduce liability for the overbilling claim substantially. But it failed to serve CMS and Palmetto prior to (or after) a hearing on plan confirmation. [8] The court confirmed the plan in the absence of objections. [9]

More than a year later, Palmetto, acting on behalf of CMS, began to exercise recoupment rights on account of the overbilling claim. [10] Unable to resolve this issue, the debtor sought and obtained entry of an order reopening its chapter 11 case and filed its complaint seeking declaratory and injunctive relief. [11]

In response, CMS filed a motion to dismiss, or alternatively, for summary judgment, "on, essentially, two main themes: ... (1) a lack of subject matter jurisdiction pursuant to the provisions of 42 U.S.C. § 405(h), and (2) [that] the Plaintiff is not entitled to [the] injunctive relief it seeks." [12] To elaborate, § 405(h) generally bars judicial review of agency action and prevents bringing an action against CMS to recover on a claim arising under the Medicare Act without first exhausting administrative remedies. [13] Thus, CMS contended that the bankruptcy court lacked jurisdiction to modify the pre-petition overbilling claim through plan confirmation because it required a determination of the amount of the claim, and that injunctive relief was unavailable to the debtor because the plan improperly modified the overbilling claim. [14]

The debtor viewed the jurisdictional issue differently. Focusing on the text of § 405(h), the debtor observed that the statute only purports to strip district courts of jurisdiction under §§ 1331 and 1346 of title 28 — not bankruptcy jurisdiction under § 1334. [15] The debtor also argued that § 405 was inapplicable to the dispute because the bankruptcy court was being asked to enforce provisions of a confirmed plan — not a claim arising under the Medicare act — and that "that Supreme Court precedent, *inter alia*, bars collateral attack of a final order when a party has failed to lodge a timely objection or appeal." [16]

In support, the debtor observed that Palmetto had sent a pre-petition letter asking to be notified of any bankruptcy filing so that the MAC could coordinate a response with CMS and the Department of Justice. [17] Thus, the debtor contended that serving CMS with notice of the bankruptcy filing "via its agent, Defendant Palmetto" was sufficient to provide CMS with an opportunity to object "to the confirmation of plaintiff's Chapter 11 Plan on the basis of lack of jurisdiction or any other basis" or to appeal the confirmation order, but that CMS "failed to do so." [18] In the debtor's view, this amounted to a waiver of CMS's § 405 jurisdictional argument.

The *La Fuente Home Health Services* Decision

The bankruptcy court agreed with the debtor that § 405 did not bar claims for enforcement of the plan against Palmetto and CMS, without resolving whether the court had jurisdiction to modify the overbilling claim under the plan. Even so, the court refused to enter summary judgment in favor of CMS on the record before it due to lingering questions about the adequacy of service.

The bankruptcy court first addressed CMS's argument that the complaint should be dismissed for lack of subject-matter jurisdiction. Rather than addressing the agency's § 405 argument, the court observed that "the *res judicata* effect of a confirmed plan can be dispositive on the necessity of resolving the potential preclusion of jurisdiction by other statutes when due process is provided to parties in interest." [19] In support, the court cited Fifth Circuit cases holding "that a chapter 11 debtor's discharge of post-petition claims was proper when the cla had actual notice of the bankruptcy" and "that a creditor's failure to timely seek bar dates after being notified of the pending bankruptcy meant the dismissal of its complaint was proper[.]" [20] In other words, "the finality of an order precludes untimely collateral attack on the jurisdiction of the court that issued that order." [21]

Turning to the service actually provided to the defendants, the bankruptcy court observed that CMS was a known creditor in this case and, based on *United Student Aid Funds Inc. v. Espinosa*, [22] that "*actual* notice of the filing and contents of [a] plan ... *more than satisfie[s]* ... due process rights." [23] That did not occur in this case, however.

Nevertheless, Palmetto was listed in the matrix, would have received official notice of the case, had requested that the debtor notify it of any bankruptcy filing for the purpose of coordinating with the government, and had received additional notice of the case from the debtor shortly after the case was filed.

Therefore, [the debtor] has satisfied the bare minimum to provide due process to Palmetto, which was statutorily obligated to "facilitate[e] communication between [the debtor] ... and the Secretary." § 1395kk-1(a)(4)(E) [and other authorities]. As such, the Court can conclude that it has subject matter jurisdiction to determine if the Plan is binding on [CMS] and Palmetto, which in turn would require the Court to interpret and, if applicable, enforce its Confirmation Order. [24]

Next, the court turned to CMS's request for summary judgment. According to the bankruptcy court, the agency's arguments were similar to those it raised in favor of dismissal under Rule 12(b)(1), and the court again found them unpersuasive. That is because the issue was "enforcement of that Plan" [25] rather than whether § 405 barred entry of the confirmation order in the first place.

While the court had denied CMS's motion to dismiss because Palmetto had actual notice of the bankruptcy case, the absence of evidence that CMS *had not* been served with plan-confirmation papers doomed the request for summary judgment. On the one hand, there was evidence suggesting, but not confirming, that CMS might have had notice of the bankruptcy case through Palmetto. [26] On the other hand, Palmetto was merely an agent for CMS, and "[w]hether Palmetto did indeed receive notice beyond the initial petition and whether such notice was provided to [CMS], as indicated [it would be in the pre-petition letter], is a significant fact upon which this dispute may very well turn, but the burden of production has not been met by the parties. [27]

Thus, the court declined to enter summary judgment for CMS because it was "unable to conclude whether Defendants had been put on notice of provisions of the Plan" prior to confirmation. [28]

Analysis

There is no doubting that the court reached the right result in the limited context before it and on these facts. However, the court's decision does not address the fact that CMS was a party entitled to its own service of process with respect to plan confirmation for the following two reasons.

First, MACs are merely fiscal intermediaries assisting CMS with the administration of a federal program; obligations under the Medicare program are owed to the federal government, not the MAC. Thus, agency regulations make clear not only that a fiscal intermediary is entitled to indemnification by the agency, but also that "CMS is the real party in interest in any litigation involving the administration of the [Medicare] program." [29] Courts agree. [30]

Second, in cases in which the debtor owes "a debt to the United States other than for taxes[,]" Bankruptcy Rule 2002(j) requires service of a disclosure statement and plan on the relevant agency *and* the "the United States attorney for the district in which the case is pending[.]" [31] In

other words, the debtor before the *La Fuente Home Health Services* court was *required* to serve CMS *and* the local U.S. attorney's office, but neglected to do so.

Conclusion

While resolution of the scope of bankruptcy jurisdiction with respect to Medicare claims will have to wait for another day, this much is clear: Health care debtors looking to bind CMS to the terms of a confirmed plan should be sure to serve CMS as well as a fiscal intermediary or MAC. Relying on the MAC to provide notice of a bankruptcy filing and contents of a plan to CMS could open the door to a collateral attack on a confirmation order in the event that such service did not provide adequate notice to the agency that its rights could be altered.

[1] Bankruptcy Case No. 7:15-bk-70265, Adv. Pro. Case No. 7:16-ap-07012, 2017 WL 1173599 (Bankr. S.D. Tex. March 28, 2017).

[2] This includes, for example, resolution of liability and repayment for pre-petition overbilling claims or post-petition agency termination of a Medicare provider agreement. For a detailed discussion of this issue, *see* Samuel R. Maizel and Michael Potere, "Killing the Patient to Cure the Disease: Medicare's Jurisdictional Bar Does Not Apply to Bankruptcy Courts," *Emory Bankruptcy Developments Journal* (Vol. 32), February 2016.

[3] *La Fuente Home Health Services Inc.,* 2017 WL 1173599, at *3.

[4] A MAC "serves as a conduit of information and payments between" the Department of Health and Human Services "and [Medicare] providers." A MAC is a type of Medicare fiscal intermediary, which is a private insurance company that acts as an agent for the federal government in the administration of the Medicare health insurance program. One of the primary responsibilities of a Medicare fiscal intermediary is to manage the payment of claims. *See* www.reference.com/government-politics/medicare-fiscal-intermediary-890ca... (last visited Nov. 29, 2017).

[5] *La Fuente Home Health Services Inc.,* 2017 WL 1173599, at *1.

[6] *Id.* at *1-*2.

[7] *Id.* at *8.

[8] *Id.*

[9] *Id.*

[10] *La Fuente Home Health Services Inc.,* Bankruptcy Case No. 7:15-bk-70265, Adv. Pro. Case No. 7:16-ap-07012, *Complaint and Application for Permanent Injunctive Relief*, Docket Entry 1, at ¶¶ 10-11 (Bankr. S.D. Tex. June 21, 2016). That a creditor could exercise a right of setoff or recoupment post-confirmation and post-discharge is not unheard of; courts have held that a creditor should be able to setoff a pre-petition debt after discharge without violating the statutory injunctive provisions of the Bankruptcy Code, without regard for the specific chapter involved. *See, e.g., In re Luongo*, 259 F.3d 323, 333 (5th Cir. 2001); *In re Deutchman*, 192 F.3d 457, 460-61 (4th Cir. 1999); *In re DeLaurentiis Entertainment Group Inc.*, 963 F.2d 1269, 1276-77 (9th Cir. 1992); *In re Davidovich*, 901 F.2d 1533 (10th Cir. 1990). *But see United States v. Continental Airlines (In re Continental Airlines)*, 134 F.3d 536 (3d Cir. 1998) (federal government could not exercise right of setoff post-confirmation of chapter 11 plan; failure to exercise right to setoff before confirmation "extinguishes" the claim.), *aff'g, In re Continental Airlines Inc.,* 218 B.R. 324 (D. Del. 1997). Similarly, courts have held that recoupment is unaffected by a discharge in bankruptcy. *In re Flagstaff Realty Assocs.*, 60 F.3d 1031, 1035-36 (3d Cir. 1995) (recoupment survives discharge even if creditor did not object to plan or seek a stay pending appeal); *In re Harmon*, 188 B.R. 421, 425 (B.A.P. 9th Cir. 1995) (recoupment "unaffected by the debtor's discharge"). *But see In re Kings Terrace Nursing Home & Health Facility*, 184 B.R. 200 (S.D.N.Y. 1995) (Medicaid recoupment is a claim within the meaning of the Bankruptcy Code; hence, a right to recoupment is barred by the discharge), *aff'g*, 1995 WL 65531 (Bankr. S.D.N.Y. Jan. 27, 1995). Courts recognize that creditors may lose such post-confirmation rights if a plan of reorganization expressly prohibits creditors from exercising any right of setoff post-confirmation and the creditor does not object or appeal. In such cases, the *res judicata* effect of the debtor's confirmed plan binds the creditor. *Compare In re Lykes Bros. S.S. Co.*, 217 B.R. 304, 311 (Bankr. M.D. Fla. 1997) (federal government bound by confirmed plan), *with In re Mirabilis Ventures Inc.,* 2011 WL 11671880 (Bankr. M.D. Fla. March 28, 2011) (where plan and confirmation order acknowledge existence of and do not specifically enjoin creditors from exercising their setoff rights, those rights survive confirmation of the plan).

[11] *La Fuente Home Health Services Inc.,* 2017 WL 1173599, at *2.

[12] *Id.* at *2.

[13] The statute, however, only expressly strips district court jurisdiction under §§ 1331 and 1346 of title 28. It does not mention § 1334, and whether this was a scrivener's error or intentional has divided federal courts.

[14] *La Fuente Home Health Services Inc.,* Bankruptcy Case No. 7:15-bk-70265, Adv. Pro. Case No. 7:16-ap-07012, *Motion of Defendant Sylvia Mathews Burwell, Secretary of the United States Department of Health and Human Services, to Dismiss Plaintiff's Complaint and Application for Permanent Injunctive Relief and/or Alternatively for Summary Judgment*, Docket Entry 19, pp. 10, 14-22 (Bankr. S.D. Tex. Aug. 9, 2016). For a discussion of the ability to obtain an injunction against the federal government is such cases, *see* Samuel R. Maizel and Judith Waltz, "Injunctive Relief in Health Care Insolvencies," 24 *California Bankruptcy Journal* 215 (1998).

[15] *La Fuente Home Health Services Inc.,* Bankruptcy Case No. 7:15-bk-70265, Adv. Pro. Case No. 7:16-ap-07012, *Plaintiff's Response and Memorandum in Opposition to Defendant's, Sylvia Mathews Burwell, Secretary of the United States Department of Health and Human Services, to Dismiss Plaintiff's Complaint and Application for Permanent Injunctive Relief and/or Alternatively for Summary Judgment*, Docket Entry 20, p. 5 (Bankr. S.D. Tex. Aug. 31, 2016) (the "Debtor's MSJ Objection").

[16] *La Fuente Home Health Services Inc.*, 2017 WL 1173599, at *2.

[17] *La Fuente Home Health Services Inc.,* Bankruptcy Case No. 7:15-bk-70265, Adv. Pro. Case No. 7:16-ap-07012, Docket Entry 19-2, p. 4 (Bankr. S.D. Tex. Aug. 9, 2016).

[18] Debtor's MSJ Objection at 8.

[19] *La Fuente Home Health Services Inc.,* 2017 WL 1173599, at *3.

[20] *Id.* at *4 (*citing Matter of Christopher*, 28 F.3d 512 (5th Cir. 1994), and *Grossie v. Sam (In re Sam)*, 894 F.2d 778 (5th Cir. 1990)).

[21] *Id.* at *3 (*citing, inter alia, United Student Aid Funds Inc. v. Espinosa*, 559 U.S. 260 (2010)).

[22] 559 U.S. 260, 272 (2010).

[23] *Id.* at *9 (*quoting Espinosa*, 559 U.S. at 272) (emphasis added). An unknown creditor might be entitled to other forms of service, such as service by publication. Either way, the objective is to provide service reasonably calculated under the circumstances to advise a party of a proceeding that it could alter its rights. *Id.* at *3.

[24] *Id.* at *10 (internal authorities omitted).

[25] *Id.* at *11.

[26] *Id.*

[27] *Id.* (internal citations omitted).

[28] *Id.* at *12.

[29] 42 C.F.R. § 421.5(b).

[30] *See Jagow v. Mutual of Omaha Ins. Co. (In re Precedent Health Center Operations LLC)*, 392 Fed. Appx. 618 (10th Cir. 2010) (affirr dismissal of Medicare provider's complaint against a fiscal intermediary for failure to exhaust administrative remedies and noting that th secretary of the U.S. Department of Health and Human Services was the real party in interest). *But see Personal Physician Care P.A. v. Physicians Trust LLC*, Case No. 6:16-cv-452-Orl-28DAB, 2016 WL 4408824 (M.D. Fla. Aug. 16, 2016) (rejecting accountable care organization's argument that the secretary was the real party in interest because the ACO was or was akin to a Medicare administrative contractor); *Zanecki v. Health Alliance Plan of Detroit*, No. 12-13234, 2013 WL 2626717, at *16 (E.D. Mich. June 11, 2013) (CMS does not remain the real party in interest when it grants a Medicare Advantage Organization the contractual right to provide Medicare benefits "likely because, as discussed, MAOs, unlike intermediaries or carriers, do not control the Secretary's purse strings.").

[31] Fed. R. Bankr. P. 2002(j).

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