PROVIDER REIMBURSEMENT REVIEW BOARD DECISION

ON THE RECORD
2003-D32

PROVIDER –
Texacare, Inc.
Duncanville, TX

Provider No. 67-7181

vs.

INTERMEDIARY – Palmetto Government Benefit Administrators/ Blue Cross Blue Shield Association

DATE OF HEARING -
April 9, 2003

Cost Reporting Period Ended
September 30, 1995

CASE NO. 98-1282

INDEX

ISSUE:

Was the Intermediary's Audit Adjustment #2 which disallowed $108,875 of Administrative and General Costs proper?

STATEMENT OF THE CASE AND PROCEDURAL HISTORY:

Texacare, Inc. ("Provider") is a private, for-profit home health agency located in Duncanville, Texas. During its cost reporting period ended September 30, 1995, the Provider had an agreement with Alamo Capital Funding of Arizona ("Alamo"), a factoring organization, to obtain financing through the transfer of its accounts receivable. The Provider also had an agreement with Medical Claims Services, Inc. during this period to obtain medical claims production, processing, and collection services. Medical Claims Services, Inc., and Alamo are related through common ownership.

Palmetto Government Benefit Administrators ("Intermediary") audited the Provider's cost report and concluded that the factoring fees paid by the Provider to Alamo were an unallowable expense. On September 26, 1997, the Intermediary issued a Notice of Program Reimbursement reflecting its disallowance of the factoring fees in the amount of $108,875. On March 4, 1998, the Provider appealed the Intermediary's disallowance (adjustment) to the Provider Reimbursement Review Board ("Board") pursuant to 42 C.F.R. §§ 405.1835-.1841 and met the jurisdictional requirements of those regulations. The amount of Medicare funds in controversy is approximately $108,437.

The Provider was represented by Donald L. Skinner, CPA. The Intermediary was represented by Bernard M. Talbert, Esq., Associate Counsel, Blue Cross Blue Shield Association.[1]

PROVIDER'S CONTENTIONS:

The Provider contends that it had to use Alamo, a factoring company, to meet its financial needs because its patient care services are practically 100 percent Medicare related. That is, because Medicare reimburses actual cost, the Provider could not generate sufficient retained earnings to meet its financing needs, and banks were unavailable for that purpose because they could not perfect a security lien on Medicare accounts receivable.[2]

The Provider contends that it charged the fees paid to Alamo and Medical Claims Services, Inc. to an account entitled Discount Factor Expense. The Provider asserts that during the term of the agreements it charged $83,036 to this account for medical claims processing and $33,916 for advance funding. Respectively, the Provider argues that the portion of the $108,875 disallowed by the Intermediary that relates to claims processing is an allowable cost subject to Medicare's reasonable cost guidelines. Moreover, the

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[1] Provider Position Paper at 1. Intermediary Position Paper at 3.

[2] Provider Position Paper at 2.

Provider argues that the portion of the disallowance that relates to advance funding should be treated as interest expense and also be allowed.

The Provider asserts that it never actually sold its receivables to Alamo; rather, the transactions were a "sale with recourse" or, in fact, a loan according to Generally Accepted Accounting Principles. The Provider explains that the transfer of its receivables to Alamo is considered a loan because it does not meet the following conditions of the Statement of Financial Accounting Standards (FAS-77):

1. The seller unequivocally surrenders to the buyer the control of the future economic benefits of the receivable. (Provider response: The agreement indicates that under certain conditions it must substitute another receivable in place of one sold.)

2. The seller's remaining obligations to the buyer must be subject to a reasonable estimation on the date of the sale of the receivable. (Provider response:
No estimate can be made on the date of the sale because the payment is subject to verification by the Intermediary.)

3. The seller cannot be required to repurchase the receivable except for some minimal amount. (Provider Response: It is required to repurchase all unpaid claims and claims not paid within a certain time period.)

In summary, the Provider contends that the Intermediary should make a distinction between its claims services costs and the costs of its advance funding of receivables. Moreover, the advance funding agreement should be considered a loan agreement and its costs treated as an allowable interest expense.

INTERMEDIARY'S CONTENTIONS:

The Intermediary contends that the issue in this case is a matter of determining whether or not the Provider's transactions with Alamo were a loan or a sale. If the transactions are determined to be a loan, then a decision must be made regarding the reasonableness and necessity of the fees paid to Alamo as interest expense.[3]

The Intermediary contends that Medicare's rules do not provide specific guidance on how to determine if a financing arrangement based upon receivables is a loan or a sale. The Intermediary explains that FAS-77 must be used to make this determination. Moreover, according to FAS-77, the Provider's transfer agreement with Alamo is, in fact, a sales agreement since it meets each of the following conditions:[4]

> 1. The seller unequivocally surrenders to the buyer the control of the future economic benefits of the receivable.

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[3] Intermediary Position Paper at 4.

[4] Exhibit I-5.

Under the agreement the Provider has no option to repurchase the receivables from Alamo. When payments are received they belong to Alamo until a break-even point is reached. For Government Receivables, the receipts are sent to a lockbox and, upon receipt, are transferred to the purchaser of the account, Alamo. The Intermediary cites page 6, paragraph 6(c) of the Healthcare Receivables Sale Agreement.[5]

The Intermediary also cites page 7 of the agreement, which states:

> [t]he Provider and ACF [Alamo] intend that the transfers of Healthcare Receivables effected pursuant to this Agreement and the applicable Assignments constitute true sales of such Healthcare Receivables by the Provider to ACF, providing ACF with the full benefits of ownership thereof, and neither the Provider nor ACF intends the transactions contemplated hereby to be, or for any purpose to be characterized as, a mere financing arrangement or as a loan from ACF to the Provider.

Healthcare Receivables Sale Agreement at 7. (Emphasis added).

The Intermediary notes that "[i]nsignificant repurchases of receivables by the seller in accordance with the recourse provisions of the transfer agreement do not preclude the recognition of a transfer of receivables from being a sale." FAS-77.

2. The seller's remaining obligations to the buyer under the recourse provisions of the transfer agreement must be subject to a reasonable estimation on the date of the sale of the receivable.

The Intermediary disputes the Provider's argument that it is difficult to estimate the receivables on the date of sale "because the payment is subject to verification by the Intermediary." The Intermediary asserts that it is a common practice for healthcare providers to verify Medicare coverage prior to furnishing services to patients or performing visits to patients' homes.

Also, on page 15 of the agreement, the Provider has virtually assured Alamo that the receivables are collectable. Therefore, the amounts of the receivable are easily determinable.

3. The seller cannot be required to repurchase the receivables from the buyer except in accordance with the recourse provisions of the transfer agreement.

The Intermediary asserts that the Provider has not shown that the repurchase of receivables has been anything other than minimal. Moreover, throughout the agreement, the Provider and Alamo consistently maintain that the intent of the transaction is to be considered a sale of accounts receivable and not a loan.

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[5] Exhibit I-1.

The Intermediary contends that the portion of the Provider's argument that pertains to Medical Claims Services, Inc. should be rejected by the Board. The Intermediary explains that the entire amount of its disallowance ($108,875) is based upon invoices generated from Alamo.[6]

Finally, and notwithstanding the fact that the Provider's transactions with Alamo were a sale of receivables and not a loan, the Intermediary rejects the Provider's argument that $33,916 of the subject disallowance should be considered allowable interest expense.[7] The Intermediary asserts that in order for interest to be allowable it must be reasonable, necessary, and proper. Pursuant to Medicare's Provider Reimbursement Manual, Part I ("HCFA Pub. 15-1") § 202, "necessary" means, in part, that interest was incurred on a loan made to satisfy a financial need, while "proper" means, in part, that interest was incurred at a rate not in excess of what a prudent buyer would pay in an arms-length transaction. Respectively, the Intermediary argues that the Provider furnished no evidence, either at the time of audit or at the time the Intermediary initiated its disallowance, that it needed to generate working capital or that it exercised due diligence in seeking financing.

FINDINGS OF FACT, CONCLUSIONS OF LAW AND DISCUSSION:

The Board, after consideration of the parties' contentions and evidence presented, finds and concludes as follows:

The Intermediary perfected an adjustment disallowing $108,875 of the Provider's costs that had been charged to an account entitled Discount Factor Expense within the Provider's accounting records. The Intermediary concluded that this amount represented factoring fees resulting from the "sale" of the Provider's health care accounts receivable to Alamo Capital Funding of Arizona. The Intermediary distinguished the transaction between the Provider and Alamo from a "loan" type of financing arrangement where the fees paid to Alamo would be considered interest expense and be allowed.

The Provider asserts that the costs charged to its Discount Factor Expense account actually stem from two different contractual arrangements and services. The Provider explains that $83,036 represents payments made to Medical Claims Services, Inc. for certain claims processing services, and that $33,916 was paid to Alamo for advance funding of Provider receivables. The Provider further asserts that the cost of claims services is an allowable expense, and that the fees paid to Alamo reflect interest expenses based upon a loan, as opposed to a sale, according to Generally Accepted Accounting Principles (FAS 77).

Accordingly, the Board finds there are two individual aspects of the subject issue to be addressed. First, it must be determined what portion, if any, of the Intermediary's adjustment pertains to claims processing services that may be allowable costs subject to Medicare's rules regarding reasonableness and necessity. Then, it must be determined if

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6 Intermediary Position Paper at 8.

7 Id.

the remaining costs, applicable to Alamo, result from the sale of the Provider's receivables or result from a loan based upon those receivables. If its determined that these costs result from a sale, they are an unallowable expense since the Provider has merely opted to receive payment prior to collection on the accounts. If, however, the fees paid to Alamo are found to result from a loan and are interest expenses, then it must be determined whether or not those costs are necessary and proper in accordance with Medicare rules.

Based upon an analysis of these matters, the Board concludes that the Intermediary's adjustment is proper. With respect to the claims processing costs at issue, the record shows that the Provider had, in fact, entered into an agreement with Medical Claims Services, Inc. to provide certain claims services during the subject cost reporting period. However, the record also shows that the Intermediary's adjustment is based solely upon invoices generated by Alamo for factoring fees. The Board finds this evidence persuasive.

Notwithstanding, the Board acknowledges that Medical Claims Services, Inc. and Alamo are commonly owned and appear to work very closely together. Moreover, the Board acknowledges a letter dated September 10, 1997, from Medical Claims Services, Inc., stating that total fees charged to/and paid by the Provider amounted to $83,036. However, the Board finds that this letter alone does not represent substantive evidence of services furnished to the Provider or payments made by the Provider and, importantly, that payments made by the Provider for claims services were commingled within Alamo's invoices. The Board is also unclear as to whether or not the entire $83,036 amount is applicable to the subject cost reporting period, i.e., October 1, 1994 to September 30, 1995. According to the Provider, the $83,036 amount applies to services furnished from November 17, 1994 (the date the agreement was entered into) to October 9, 1995 (the date of termination). According to the letter itself, the $83,036 pertains to services rendered from "9/94 to 10/95." And, while both the Provider and Intermediary agree that $108,875 was charged to the Provider's Discount Factor Expense account, and that that amount was disallowed by the Intermediary, the Provider's figures add to a total of $116,952 ($83,036 + $33, 916), not $108,875.

Having concluded that all costs at issue in this case pertain to factoring fees paid to Alamo, the Board further finds that these costs result from the sale of the Provider's accounts receivables rather than from a loan based upon those receivables. The Board acknowledges the Provider's argument that its agreement with Alamo does not meet the three (3) conditions set forth in FAS 77 to qualify the transfer of its receivables as a sale. However, the Board, while agreeing that FAS 77 furnishes the principles to be applied in this instance, disagrees with the Provider's conclusion. The Board finds that a simple reading of the subject agreement shows that the Provider sold its receivables; that Alamo controlled the future economic benefit of the receivables; that there was reasonable estimation of the value of the receivables at the date of sale; and that the Provider was not required to repurchase the receivables except in limited circumstances. For example, the subject agreement states:

2. SALE, TRANSFER AND ASSIGNMENT TO ACF [Alamo]

(a) The Provider hereby sells, transfers, conveys and assigns to ACF all of the Provider's right, title and interest in and to all Healthcare Receivables as are accepted by ACF for purchase hereunder, together with all replacements and proceeds, thereof, and all right, title and interest of the Provider. . . .

(b) AFC's rights with respect to the Healthcare Receivables purchased hereunder include, but are not limited to, the right to: (i) sell, assign, transfer, pledge, encumber, settle, and/or compromise any or all of such Healthcare Receivables;

(c) This agreement is intended to, and does, evidence a seller and purchaser relationship between ACF. . . , and the Provider. . . , and shall be interpreted to accomplish such in all events. Both parties hereto agree to modification and reformation of their rights. . . , to avoid classification of the Agreement, and the relationship between ACF and the Provider created hereby, as a mere financing arrangement.

Healthcare Receivables Sale Agreement at 1.

DECISION AND ORDER:

The Intermediary's adjustment disallowing the Provider's factoring fees expenses is proper. The Intermediary's adjustment is affirmed.

Board Members Participating:

Suzanne Cochran, Esq. (Recused)
Henry C. Wessman, Esq.
Dr. Gary B. Blodgett
Martin W. Hoover, Jr., Esq.
Elaine Powell

DATE: June 12, 2003

FOR THE BOARD:

Suzanne Cochran, Esq.
Chairman