PROVIDER REIMBURSEMENT REVIEW BOARD DECISION

2015-D2

PROVIDER –
St. Vincent – Randolph Hospital, Inc.

Provider No.: 15-1301

vs.

INTERMEDIARY –
Wisconsin Physician Services/
Blue Cross and Blue Shield Association

DATE OF HEARING -
February 11, 2014

Cost Reporting Periods Ended –
2004-2008

CASE NOs.: 06-1843
07-1701
08-1543
10-0786
10-1178

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ISSUE:

Was the Intermediary's disallowance of the interest expense proper for St. Vincent Randolph for the 2004, 2005, 2006, 2007 and 2008 fiscal years? [1]

MEDICARE STATUTORY AND REGULATORY BACKGROUND:

This is a dispute over the amount of Medicare reimbursement due a provider of medical services.

The Medicare program was established under Title XVIII of the Social Security Act, as amended ("Act"), to provide health insurance to eligible individuals. Title XVIII of the Act was codified at 42 U.S.C. Chapter 7, Subchapter XVIII. The Centers for Medicare & Medicaid Services ("CMS"), formerly the Health Care Financing Administration ("HCFA"), is the operating component of the Department of Health and Human Services ("DHHS") charged with administering the Medicare program. CMS' payment and audit functions under the Medicare program are contracted to organizations known as fiscal intermediaries ("FIs") and Medicare administrative contractors ("MACs"). FIs and MACs[2] determine payment amounts due the providers under Medicare law, regulation and interpretative guidelines published by CMS.[3]

Cost reports are required from providers on an annual basis with reporting periods based on the provider's accounting period. A cost report shows the costs incurred during the relevant period and the portion of those costs to be allocated to Medicare.[4] The intermediary reviews the cost report, determines the total amount of Medicare reimbursement due the provider, and issues the provider a Notice of Program Reimbursement ("NPR").[5] A provider dissatisfied with the intermediary's final determination of total reimbursement may file an appeal with the Provider Reimbursement Review Board ("Board") within 180 days of the receipt of the NPR.[6]

Interest expense is generally not allowable unless it is incurred on "indebtedness established with lenders or lending organizations not related through control, ownership, or personal relationship to the borrower."[7] Specifically Medicare regulations at 42 C.F.R. § 413.153(c)(1) state in pertinent part:

> (c) *Borrower-lender relationship*. (1) Except as described in paragraph (c)(2) of this section, to be allowable, interest expense must be incurred on indebtedness established with lenders or lending organizations not related through control, ownership, or personal relationship to the borrower. Presence of any of these factors could affect the 'bargaining' process that usually accompanies the making of a loan, and could thus be suggestive of

[1] The parties stipulated to this issue statement and the Provider withdrew its appeal of fiscal year 2002 (Case No. 04-0953) at the February 11, 2014 hearing. *See* Transcript ("Tr.") at 8:24-9:5.
[2] FIs and MACs are hereinafter referred to as intermediaries.
[3] *See* 42 U.S.C. §§ 1395h, 1395kk-1; 42 C.F.R. §§ 413.20, 413.24.
[4] *See* 42 C.F.R. § 413.20.
[5] *See* 42 C.F.R. § 405.1803.
[6] *See* 42 U.S.C. § 1395oo(a); 42 C.F.R. §§ 405.1835-1837.
[7] *See* 42 C.F.R. § 413.153.

> an agreement on higher rates of interest or of unnecessary loans. Loans should be made under terms and conditions that a prudent borrower would make in arm's length transactions with lending institutions. The intent of this provision is to assure that loans are legitimate and needed, and that the interest rate is reasonable. Thus, interest paid by the provider to partners, stockholders, or related organizations of the provider would not be allowable. . . .

However, if a Medicare provider is operated by members of a religious order and borrows from the order, the interest is allowable as explained in (c)(2) of the regulation:[8]

> Exceptions to the general rule regarding interest on loans from controlled sources of funds are made in the following circumstances. . . . In addition, if a provider operated by members of religious order borrows from the order, interest paid to the order is an allowable cost.

This exception is referred to as the "Motherhouse" exception. Section 220 of the Provider Reimbursement Manual, CMS Pub. No. 15-1 ("PRM 15-1") expands on the Motherhouse exception by stating:

> Providers owned and operated by members of religious orders often obtain funds through loans from the Mother House or Governing Body of the religious order. Where there is a contractual agreement for the payment of interest and for the eventual repayment of the loan, the interest expense is allowable as cost provided the interest is applicable to the period after the certification of the institution as a provider. Interest expense incurred during a reporting period must be paid within the succeeding reporting period.

PRM 15-1 § 202.1 further explains for interest to be allowable, it must be:

- Supported by evidence of an agreement that funds were borrowed and that payment of interest and repayment of the funds are required;
- Identified in accounting records;
- Related to the reporting period in which the costs are incurred; and
- Necessary and proper for the operation, maintenance, or acquisition of facilities.

[8] *See* 42 C.F.R. § 413.153(c)(2).

STATEMENT OF THE CASE AND PROCEDURAL HISTORY:

This is a dispute about whether St. Vincent Randolph Hospital ("St. Vincent Randolph") met the documentation requirements necessary to claim reimbursement for interest that it paid during fiscal years ("FYs") 2004 to 2008 in conjunction with a series of loans and bond financing transactions related to the construction of its new facility.[9] St. Vincent Randolph claims that the "Motherhood exception" applies to its loan from Ascension Health, a Catholic nonprofit health system, and that it has submitted sufficient documentation to support its claim for reimbursement of interest expense for FYs 2004 to 2008. St Vincent Randolph claims that Wisconsin Physicians Service Insurance Corporation, its designated intermediary ("Intermediary"), erred in removing the interest expense from its cost reports for FYs 2004 to 2008.

The Board conducted a hearing on February 11, 2014. St. Vincent Randolph was represented by Daniel Miller, Esq. and Elizabeth A. Elias, Esq. of Hall Render Killian Heath & Lyman, P.C. The Intermediary was represented by Robin Sanders, Esq. of the Blue Cross and Blue Shield Association.

PROVIDERS' CONTENTIONS:

St. Vincent Randolph asserts that the loan from Ascension Health qualifies as a Motherhouse Loan and that it has submitted sufficient documentation to claim reimbursement for the interest it paid.

St. Vincent Randolph Hospital is licensed by the State of Indiana and is a corporate subsidiary of St. Vincent Health, which itself is a subsidiary of Ascension Health. Ascension Health was formed in November 1999 by the following Roman Catholic Religious orders: the Daughters of Charity of St. Vincent de Paul, the Sisters of St. Joseph of Nazareth, and the Congregation of the Sisters of St. Joseph of Carondelet.[10]

St. Vincent Health began the process of acquiring the former Randolph County Hospital in 1999. It formed St. Vincent Randolph Hospital, Inc., an Indiana nonprofit corporation, with St. Vincent Health designated as its sole corporate member. At the same time St. Vincent Randolph was incorporated to become the operator of the former county hospital, St. Vincent Health was also operating another hospital, St. Vincent Hospital & Health Care Center (referred to as St. Vincent Indianapolis).[11]

Shortly after St. Vincent Randolph became affiliated with St. Vincent Health, St Vincent Randolph borrowed funds to construct a new facility.[12] St. Vincent Health facilitated a related parties loan transaction whereby, in 2002, St. Vincent Indianapolis loaned St. Vincent Randolph $15.5 million for the construction of St. Vincent Randolph's new facility.[13] The Executive Director of Operations ("EDO") for St Vincent Health, stated during the hearing that the intent of

[9] *See* Medicare Administrative Contractor's Post Hearing Brief at 1.
[10] *See* Providers Consolidated Final Position Paper at 1.
[11] *See id.* at 1 - 2.
[12] *See id* at 2.
[13] *See* Provider's Post-Hearing Brief at 2; Tr at 28:7-14.

the St. Vincent Indianapolis loan was to be short term financing, so that long term debt financing could be arranged.[14] The related parties never documented the full terms of this loan agreement.[15]

In 2003, St. Vincent Randolph became an obligated member of the Ascension Health Obligated Group ("Obligated Group").[16] As a member of the Obligated Group, St. Vincent Randolph was able to participate in the Ascension Health Bond Financing Program. Through its membership in this Obligated Group, St. Vincent Randolph incurred a debt of $15,568,979.88.[17] At the hearing, St. Vincent Randolph's EDO testified that this new debt was used to repay the 2002 loan, between St. Vincent Indianapolis and St. Vincent Randolph.[18] St. Vincent Randolph asserts that the 2002 interim loan from its sister hospital, does not disqualify it from claiming reimbursement for subsequent years interest payments, made on the new debt.[19] St. Vincent Randolph maintains that the Board should conclude that the Motherhouse exception applies to the cost report years in this appeal consistent with the Board's findings in *All Saints Hosp. v. Blue Cross Blue Shield Ass'n*, PRRB Dec. No. 1979-D63 (Oct. 9, 1979).[20] In that decision the Board held that a loan from Episcopal Community Services of the Episcopal Diocese of Pennsylvania ("ECS") qualified for the Motherhouse exception. Similarly, St. Vincent Randolph points to the Board's decision in *Saint Elizabeth Hosp. v. Blue Cross and Blue Shield Ass'n*, PRRB Dec. No. 1993-D91 (Sept. 17, 1993), *modified* CMS Administrator Dec. (Nov. 17, 1993).[21] Therein, the Board upheld the claim for interest even though the provider had not paid cash to its religious sponsor. Rather, the provider had transferred real estate to its sponsor, and the Board determined that transfer also satisfied the Motherhouse exception.
In addition, St. Vincent Randolph notes that federal courts have considered issues related to loans among religious orders and upheld the propriety of claiming interest expense for such loans. For example, the U.S. District Court for the District of Columbia ruled in favor of reimbursement under the Motherhouse exception in *Cabrini Medical Center v. Schweiker*, No. 80-2740, CCH Medicare and Medicaid Guide 1981 Transfer Binder ¶ 30,961 (D.D.C. Mar. 25, 1981).[22] In addition, the U.S. Court of Appeals for the Seventh Circuit held in *Hinsdale Hosp. Corp. v. Shalala*, 50 F.3d 1395 (7th Cir. 1995) ("*Hinsdale*") that, while a loan between brother-sister hospitals did not constitute a loan from a Motherhouse, a loan from the corporate parent would qualify.[23] The St. Vincent Randolph asserts that the corporate structure in the Seventh Circuit referred to in *Hinsdale* was very similar to the structure in which St. Vincent Randolph operates.

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[14] Tr. at 28:15-21. *See also id.* at 32:9-19. .
[15] *See* Provider Exhibit P-1 at SVR-0002-SVR-006; Tr. at 44:1-25.
[16] Tr. at 33:21-34:4. *See also* Provider Exhibit P-2 at SVR-0058.
[17] Tr. 39-2-22. *See also* Provider Exhibit P-2 at SVR-0096 (Schedule 1 to December 31, 2003 "Contribution Agreement" between St. Vincent – Randolph and Ascension Health).
[18] Tr. at 39:16-40:10.
[19] Provider's Post Hearing Brief at at 5.
[20] Copy included at Provider Exhibit P-32.
[21] Copy included at Provider Exhibit P-33. The Board also reached the same conclusion in an earlier case involving that same provider. *See Saint Elizabeth Hosp. v. Blue Cross Blue Shield Ass'n*, PRRB Dec. 1992-D64 (Sept. 18, 1992).
[22] Copy included at Provider Exhibit P-34.
[23] Copy included at Provider Exhibit P-35.

St. Vincent Randolph contends that the Motherhouse exception clearly applies to the interest payments St. Vincent Randolph made to Ascension Health during FYs 2004 through 2008. St. Vincent Randolph became part of the Ascension Health bond financing group in 2003. The fact that Ascension Health issued bonds in 2002, 2003 and in 2005 to provide for the financial needs of St. Vincent Randolph, as well as its other affiliated hospitals, underscores the fact that the Motherhouse exception applies to the interest expense St. Vincent Randolph paid to Ascension Health in FYs 2004 - 2008.

St. Vincent Randolph maintains that it has documented the loan per 42 C.F.R § 413.24. Beginning in 2003 and from that point forward, there is complete documentation on all aspects of the debt, as well as payments of the interest that St. Vincent Randolph claimed on its Medicare cost reports.[24] In addition, St. Vincent Randolph asserts that it has submitted documentation, including audited financial statements and tax forms, supporting the 2003 repayment of the 2002 loan from St. Vincent Indianapolis.[25]

St. Vincent Randolph contends that it has provided documentation to support the allowability of the interest expense as a Motherhouse loan. Additionally, St. Vincent Randolph claims it followed the requirement of PRM 15-1 § 220 including paying all of the interest within the year in question or the succeeding cost reporting period.

INTERMEDIARY'S CONTENTIONS:

The Intermediary conducted a full desk review in March 2007, concluding that numerous adjustments would be required. St. Vincent Randolph borrowed money during FY 2002 from its "sister hospital", St. Vincent Indianapolis, to build a new hospital. The Intermediary disallowed the interest expense related to this loan on the basis that it was between related parties and not properly documented. Subsequently, St. Vincent Randolph replaced this loan through a loan with Ascension Health.[26] The Intermediary contends that St. Vincent Randolph cannot restructure the loan to cure the related party issues.

The Intermediary argues that the Ascension Health loan, financed through publicly-placed bonds with unrelated parties, does not change the structure of the original loan and, therefore, the interest expense does not meet the related party exclusion. The Intermediary asserts that St. Vincent Randolph's replacement note was created for the sole purpose of making the interest expense allowable for Medicare purposes and not the Provider's actual "financial need."[27]

The Intermediary contends that St. Vincent Randolph bears the burden of proving, by a preponderance of the evidence, that it is entitled to the claimed interest expense under the applicable rules and regulations. In particular, St. Vincent Randolph must demonstrate that the 2003 refinancing actually repaid the 2002 loan between the related parties St. Vincent Randolph

[24] *See* Provider Exhibits P-2, P-3, P-41 – P-44.
[25] *See* Provider's Post Hearing Brief at 4-5. *See* also Provider Exhibits P-56 – P-64.
[26] Intermediary Exhibit I-1.
[27] Medicare Administrative Contractor's Final Position Paper at 6.

and its sister hospital, St. Vincent Indianapolis. The Intermediary argues that St. Vincent Randolph has failed to provide the documentation to satisfy its burden of proof.

FINDINGS OF FACT, CONCLUSIONS OF LAW AND DISCUSSION:

After considering the facts, controlling Medicare law and regulations, the evidence presented, the parties' contentions, and post-hearing briefs, the Board concludes that St. Vincent Randolph properly claimed interest expense on its Medicare cost report for FYs. 2004 through 2008.

The issues for the Board to decide in this case are: 1) whether changing the source of a loan from a related party to a religious order cures the "borrower-lender relationship" prohibition at 42 C.F.R. § 413.153(c) making the interest expense an allowable cost from that point forward based on the Motherhouse exception in (c)(2) of the regulation; and 2) if so, whether St. Vincent Randolph submitted sufficient documentation to support reimbursement for the interest it paid on the loan from Ascension Health.

The Board finds that the regulations governing Medicare reasonable cost reimbursement, including those at 42 C.F.R. § 413.153(c), neither prohibit nor preclude a provider from changing the source of its borrowed funds. Further, the Board finds that these regulations do not prohibit the curing of a nonallowable related-party interest expense through refinancing of the loan with a third party lender or Motherhouse. Therefore the Board concludes that the loan between St. Vincent Randolph and Ascension Health qualifies under the "Motherhouse" exception at 42 C.F.R. § 413.153(c)(2).

The Board next applied the Motherhouse exception to this case. The Board finds that there is sufficient evidence to document that the original loan between St. Vincent Randolph and St. Vincent's Hospital Indianapolis was paid off as of July 1, 2003, thereby curing the tainted funds.[28] The Board also finds that there is sufficient evidence to document that Ascension Health qualifies as a Motherhouse and that Ascension Health made the loan at issue to St. Vincent Randolph.[29] As such, the Board concludes that the interest that St. Vincent Randolph paid on the loan from Ascension Health is an allowable cost.

DECISION AND ORDER:

The Board finds that the Intermediary's disallowance of interest expense for St. Vincent Randolph's cost reporting periods for fiscal years 2004 to 2008 was improper. The Intermediary's adjustments are reversed.

BOARD MEMBERS PARTICIPATING:

Michael W. Harty
Clayton J. Nix, Esq.
L. Sue Andersen, Esq.
Charlotte F. Benson, CPA

[28] *See* Provider Exhibit P-57 at Tabs A to D.
[29] *See* Provider Exhibits P-2, P-3, P-4, P-41 – P-44, P-56 – P-64.

FOR THE BOARD:

/s/
Michael W. Harty
Chairman

DATE: FEB 05 2015