MEMORANDUM

TO: HEALTH CARE CLIENTS
DATE: February 15, 2002
RE: U.S. Supreme Court Denies Petitions to Review
“One Purpose” Test under the Anti-Kickback Statute

On January 7, 2002, the United States Supreme Court denied petitions for writs of certiorari filed by certain defendants in the widely observed Kansas City Anti-Kickback prosecutions. The petitions sought review of two appellate decisions upholding convictions under the Anti-Kickback Statute involving arrangements between a physician group and Baptist Medical Center (“Baptist”). By denying the petitions, the Court preserved the June 13, 2000 and August 17, 2001 decisions of the United States Court of Appeals for the Tenth Circuit sustaining the criminal convictions of physicians and hospital executives. Perhaps the most notable and widely criticized impact of this recent development is to let stand the broad “one purpose” test for determining whether a defendant violated the Anti-Kickback Statute.

I. FACTUAL BACKGROUND

Doctors Robert and Ronald LaHue served as principals in Blue Valley Medical Group (“BVMG”), a specialized practice group that provided medical care to patients in nursing homes and other residential care facilities. In 1984, the LaHues allegedly approached Baptist regarding the possible acquisition of BVMG in exchange for moving BVMG patients from other hospitals to Baptist. The acquisition never transpired; however, in January 1985, Baptist entered into a one-year agreement with the LaHues under which each doctor was paid $75,000 per year to act as a Co-Director of Gerontology

42 U.S.C. § 1320a-7b(b).
Services at Baptist. According to the record, the LaHues then began referring BVMG nursing home patients who required hospital care to Baptist.

According to Tom Eckard, an employee who was hired to act as a liaison between Baptist and BVMG, during the first year of the contractual relationship, the LaHues provided “minimal to no services to Baptist.”3 Ronald Keel, a neighbor of Ronald LaHue, was a Vice President at Baptist whose responsibilities included monitoring the relationship between Baptist and BVMG. In January 1986, Keel recommended modifying the agreement with the LaHues to accurately reflect the services the LaHues were providing. He also recommended reducing the annual payments from $75,000 to $50,000 each. Dan Anderson, Baptist’s Chief Executive Officer, approved the recommendation to specify precisely the LaHues’ services, but wanted to “discuss” Keel’s recommendation to reduce the fees.4 In June 1986, the contract between BVMG and Baptist was renewed for another year at $75,000 each.

In March 1991, as a result of the merger between Baptist and Health Midwest, new legal counsel reviewed Baptist’s contract with BVMG. Later that year, Baptist’s attorneys, Mark Thompson and Ruth Lehr, began discussing ways to draft a new contract with the LaHues to bring the relationship within Anti-Kickback Statute safe harbor regulations, which recently had been promulgated by the Health and Human Services Office of the Inspector General. During that period, Lehr sent a letter to the LaHues about restructuring the agreement in which she wrote, “[I]t is absolutely essential that there be no documentation of any intent to refer patients” – phraseology that was quoted in the indictment to support the charge that she sought to cover up an illegal deal. In the summer of 1991, Keel suggested that BVMG (rather than Baptist) employ Eckard, that the contract be modified to direct patients to hospitals within specified postal zip codes, and that the hospital increase the amount of fees paid to the LaHues by $70,000, the amount of Eckard’s salary. Keel directed his suggestions to McClatchey, who forwarded them to hospital lawyers. The hospital did not adopt the recommendations. Furthermore, in the process of negotiating eleven different drafts of the contract, the LaHues rejected a provision that would have required them to perform a minimum number of service hours for Baptist. A contract was eventually executed in 1993 (the “1993 Contract”).

According to testimony presented at trial, in late 1991 or early 1992, McClatchey and others learned that the LaHues had failed to perform some of the services required by the contract and that certain medical staff members at Baptist were not even interested in having such services performed by the LaHues. As a consequence, McClatchey and Thompson discussed concerns that the LaHues were not performing sufficient services to justify their fees.

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On November 5, 1992, an FBI agent and Medicaid Fraud Investigator visited Baptist and spoke with McClatchey and Anderson about Baptist’s relationship with BVMG. Notwithstanding, Baptist negotiated two subsequent temporary agreements that sustained payments to the LaHues through June 1994.

II. LEGAL PROCEEDINGS

A. Physicians, Hospital Executives and Attorneys Indicted and Tried

On July 15, 1998, a grand jury returned a twelve-count superseding indictment against the LaHues, Anderson, McClatchey, Keel, Thompson and Lehr. The indictment alleged a scheme and conspiracy to solicit, receive and pay $2.2 million in bribes for patient referrals. The indictment charged that the LaHues referred Medicare and Medicaid patients to five hospitals in Kansas and Missouri, including Baptist, and that the hospitals paid kickbacks for the referrals. According to the indictment, the kickbacks were disguised as fees under sham consulting agreements. Prosecutors claimed that the indicted local hospital attorneys conspired with the principals to craft the agreements to cloak an illegal arrangement. Also named as unindicted co-conspirators were two Baltimore attorneys in a firm with a national health law practice, who were apparently consulted in the matter. The case received national attention partly because it was the first indictment of health care attorneys under the Anti-Kickback Statute.

The case proceeded to trial, and in March 1999, at the close of the government’s case, the district court granted the attorney defendants’ motions for acquittal, finding that a reasonable jury could not conclude from the evidence presented that the attorneys had prepared sham agreements to conceal a fraud. Acknowledging ambiguity in the language and interpretation of the Anti-Kickback Statute, the court found that “[i]t is undisputed from the evidence that all the lawyers who dealt with or reviewed these transactions … held good faith beliefs that it was possible to facilitate some business relationship that was legal between the hospitals and BVMG.”

At the end of the trial, which continued as to the other defendants, the district court issued jury instructions, which included the following charge with respect to the Anti-Kickback Statute:

In order to sustain its burden of proof against the hospital executives for the crime of violating the Anti-Kickback Statute, the government must prove beyond a reasonable doubt that the defendant under consideration offered or paid remuneration with the specific intent “to induce” referrals. To offer or pay remuneration to induce referrals means to offer or pay remuneration with the intent to gain influence over the reason or judgment of a person making referral decisions. The intent to gain such influence must, at least in part, have been the reason the remuneration was offered or paid.
The jury convicted the LaHues, Anderson and McClatchey of conspiring to violate the Anti-Kickback Statute. The jury acquitted Keel on statute of limitations grounds, concluding that he withdrew from the conspiracy in 1992 when he left Baptist for another job. Following the conviction, the defendants filed various post-trial motions with the district court.

B. District Court Upholds Some Convictions and Overturns Another

On July 21, 1999, the district court granted McClatchey’s motion for acquittal, and in the alternative, for a new trial. In the same opinion, the court denied acquittal motions from Anderson and the LaHues. Based on the language of the Anti-Kickback Statute, the court found that there was “ample evidence to support the inference that both Robert LaHue and Ronald LaHue acted with a bad purpose, specifically intending to violate the Anti-Kickback Act at Baptist Hospital.” The court observed that, from the beginning, the relationship between Baptist and BVMG was “about patients and what Baptist would have to do for the LaHues in order to obtain referrals.” The opinion also noted that as soon as the LaHues started receiving $150,000 per year from Baptist, the doctors each began referring large numbers of patients to Baptist, away from other hospitals they had previously used. The opinion pointed to evidence indicating that the LaHues performed very few services in return for the substantial sum they received each year from Baptist. Accordingly, the court held that, “[a] reasonable jury could conclude from this evidence that the LaHues solicited and received considerable sums of money from Baptist, intending to be influenced by that money in their patient referral decisions.”

As for Dan Anderson, the issue before the district court was whether his actions demonstrated that he caused Baptist to pay more than fair market value for consulting services, whether he knew the consulting services were illegitimate, and whether he knew that they were not being performed adequately. The court found that the government’s evidence was sufficient on all counts and refused to grant Anderson’s petition for acquittal.

Finding that McClatchey’s role differed significantly from Anderson’s and the LaHues’ insofar as it was Anderson who offered to pay the doctors, the district court overturned the jury’s conviction of McClatchey. The court found that “McClatchey played only a peripheral role in the alleged offer and payment scheme because there is simply no evidence that he personally offered or paid or directed any remuneration to induce referrals” and consequently “the government can obtain a conviction only on a coconspirator liability theory.” The court concluded that the evidence presented was insufficient for a reasonable jury to find that he deliberately joined a conspiracy specifically intending to do something the law prohibits.
C. Appeals Court Reverses District Court Acquittal of McClatchey

The government appealed both the judgment of acquittal and the alternative grant of a new trial for McClatchey. On June 13, 2000, the U.S. Court of Appeals for the Tenth Circuit reversed both rulings in a much-anticipated and widely criticized decision. The opinion stated that the Court of Appeals disagreed with the district court’s assessment of the evidence concerning McClatchey’s negotiation of the 1993 Contract with the LaHues. The court found that, “[a]lthough it may be true that the 1993 contract appears to encompass a legal arrangement, the evidence supports a reasonable inference that McClatchey would never have supported negotiating and entering into that contract absent his intent to induce the LaHues to continue referring their patients to Baptist.”

More significantly however, the Court of Appeals also rejected McClatchey’s arguments for affirming the district court’s grant of a new trial based on the notion that the lower court improperly instructed the jury that it could convict McClatchey if remuneration was paid “at least in part” to induce patient referrals.

D. Appeals Court Affirms “One Purpose” Test

The issue of whether the “one purpose” standard constitutes the correct interpretation of the Anti-Kickback Statute was before the Tenth Circuit for the first time in the McClatchey appeal. McClatchey contended that the jury instruction with respect to the intent to induce referrals under the Anti-Kickback Statute was improper and therefore he was entitled to a new trial. This issue was not the central issue raised by McClatchey, but the Tenth Circuit nevertheless took it up, explicitly rejecting McClatchey’s requests to submit a brief on the “one purpose” test.

McClatchey argued that the instruction to the jury was incorrect because a defendant should not be convicted under the Anti-Kickback Statute when his offer or payment of remuneration was motivated merely in part to induce referrals, but rather, in order to convict, the motivation to induce referrals must be the primary purpose. He urged that the jury instruction was overly broad because “every business relationship between a hospital and a physician is based ‘at least in part’ on the hospital’s expectation that the physician will choose to refer patients.” The court rejected McClatchey’s argument. The opinion cited United States v. Greber, 760 F.2d 68, 69 (3d. Cir. 1985), which held that “if one purpose of the payment was to induce referrals, the [Anti-Kickback Statute] has been violated.” However, the Tenth Circuit arguably articulated an even broader test when it stated that “a hospital or individual may lawfully enter into a business relationship with a doctor and even hope for or expect referrals from that doctor, so long as the hospital is motivated to enter into the relationship for legal reasons entirely distinct from its collateral hope for referrals.” Since the jury instruction was consistent with that legal standard, the court rejected McClatchey’s request for a new trial based on the argument that the jury instruction was erroneous.
On August 17, 2001, the Tenth Circuit affirmed the convictions of Anderson and the LaHues, finding that it was bound by the court’s earlier ruling on the “one purpose” test in the McClatchey case, and rejecting arguments that the Anti-Kickback Statute is unconstitutionally vague.\textsuperscript{5} Anderson and the LaHues challenged the jury instructions given at their trial, specifically in regard to the “one purpose” standard. Similar to McClatchey, they argued that conviction under the Anti-Kickback Statute is only appropriate when the motivation to induce or in return for referrals was the defendant’s primary purpose. The Court of Appeals held that it was “bound by the precedent of prior panels absent en banc reconsideration or a superseding contrary decision by the Supreme Court.” Since defendants’ petition for an initial hearing by a full panel of the appeals court was denied, and the Supreme Court had not, in the interim, decided a case that required a different conclusion, the court held that it was bound by McClatchey decision as controlling authority. As a result, the court ruled that the jury instructions given “accurately informed the jury of the law applicable to Mr. Anderson.”

With respect to the LaHues, the Court of Appeals concluded that “the reasoning underlying the McClatchey holding applies equally to remuneration solicited or received in return for Medicare or Medicaid patient referrals.” In support of the decision, the opinion explained that, “[a]s a practical matter, if we held otherwise, we could illogically be faced with a case in which the offeror/payor is deemed to violate the Act, but the offeree/payee is not.” Thus the court held that the jury instructions relevant to the LaHues were proper.

\textbf{III. PETITION TO THE U.S. SUPREME COURT}

The LaHues and Anderson subsequently sought review of the Tenth Circuit’s decision by the U.S. Supreme Court. The Supreme Court has yet to address directly the propriety of the “one purpose” test in interpreting and applying the prohibitions of the Anti-Kickback Statute. Five hospital and medical associations filed an \textit{amicus curiae}, or friend of the court, brief in support of Supreme Court review of the “one purpose” test.\textsuperscript{6} The brief urged the Supreme Court to interpret the Anti-Kickback Statute to prohibit only those financial arrangements that have the primary purpose of inducing referrals. The associations argued that such an interpretation would allow “vigorous enforcement against corrupt arrangements, yet not criminalize everyday beneficial practices that inherently involve referrals but which Congress never intended to prohibit.” The group contended that the fundamental flaw with the “one purpose” test is that it ignores the existence of referrals as part of most hospital-physician

\textsuperscript{5} United States v. LaHue et al., 261 F.3d 993 (10th Cir. 2001).
\textsuperscript{6} The brief was filed by the American Hospital Association, the Federation of American Health Systems, the Association of American Medical Colleges, the American Osteopathic Association, and the Missouri Hospital Association.
interactions and thus its treats in the same manner arrangements that, by definition, have a referral component as it does those arrangements where payments are deliberately and primarily intended to induce referrals.

Notwithstanding broad support within the health care industry for a narrowing of the “one purpose” test, as evidenced by the organizations that contributed to the amicus curiae brief, the Supreme Court denied the defendants’ petition for review. As a result, the “one purpose” test remains the law in the Tenth Circuit.

IV. CONCLUSION

This development has widespread implications for those seeking to ensure that arrangements between referral sources and referral recipients will not result in criminal prosecution under the Anti-Kickback Statute. Unless a transaction fits within statutory exception to the Anti-Kickback Statute or a regulatory safe harbor, or the parties have obtained a favorable advisory opinion, there is seemingly no assurance that a transaction could not be assailed as violating the law on the basis that some minor motivating factor involves referrals. Therefore, providers must exercise a high degree of care to ensure that decisions concerning business arrangements are “entirely free” of any collateral hope for referrals. Among other things, this may suggest careful documentation of the legitimate reasons for the business arrangements, and educating all persons involved as to the legal motives for the transaction to avoid misunderstanding of the role of any referrals in the decisionmaking. In many cases, solid documentation that the transaction is based on fair market value will go a long way, but under the “one purpose” test, this alone is insufficient. Parties are well-advised to monitor business relationships to ensure that assumptions material to a conclusion that a transaction is legally compliant are borne out, including by substantiating in writing that the items and services covered by the transaction were necessary and actually provided.

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