PROVIDER REIMBURSEMENT REVIEW BOARD DECISION

2011-D6

PROVIDER –
UPMC 2003-2006 Count of FTE Residents CIRP Groups
Pittsburgh, Pennsylvania

Provider Nos.: Various (See Appendix I)

vs.

Medicare Administrative Contractor -
BlueCross BlueShield Association/ Highmark Medicare Services

DATE OF HEARING -
October 15, 2009

Cost Reporting Periods Ended - June 30, 2003, June 30, 2004, June 30, 2005 and June 30, 2006

CASE NOs.: 05-0508G, 06-0784G, 07-0510G and 08-1412G

INDEX

ISSUE:

Whether the Intermediary/Medicare Administrative Contractor properly calculated the Providers' 1996 resident cap for purposes of direct graduate medical education and indirect graduate medical education payments.

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 to provide health insurance to the aged and disabled. 42 U.S.C. §§1395-1395cc. 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 (FI) and Medicare Administrative Contractors (MAC). FIs and MACs determine payment amounts due the providers under Medicare law, regulation and interpretative guidelines published by CMS. 42 U.S.C. §1395h, 42 C.F.R. §§413.20 and 413.24.

At the close of its fiscal year, a provider must submit a cost report to the FI or MAC showing the costs it incurred during the fiscal year and the portion of those costs to be allocated to Medicare. 42 C.F.R. §413.20. The FI or MAC reviews the cost report, determines the total amount of Medicare reimbursement due the provider and issues the provider a Notice of Program Reimbursement (NPR). 42 C.F.R. §405.1803. A provider dissatisfied with the FI's or MAC's final determination of total reimbursement may file an appeal with the Provider Reimbursement Review Board (Board) within 180 days of the issuance of the NPR. 42 U.S.C. §1395oo(a); 42 C.F.R. §§405.1835 - 405.1837.

Medicare reimburses a teaching hospital for its share of costs associated with direct graduate medical education (DGME) and indirect medical education (IME). 42 U.S.C. §§1395ww(h) and 1395ww(d)(5)(B). The Secretary pays providers an additional payment for DGME costs determined under regulations at 42 C.F.R. §§ 413.75 through 413.83.[1] The amount of the DGME payments, to some extent, depends on the number of full-time equivalent (FTE) residents in the provider's residency training programs. The Secretary also pays providers an additional payment for IME determined under regulations at 42 C.F.R. §412.105. The amount of IME payment also depends partly on the number of FTEs in the provider's residency programs.

In §§4621 and 4623 of the Balanced Budget Act of 1997 (BBA), Pub. L. No. 105-33 (August 5, 1997), 42 U.S.C. §§1395ww(h)(4)(F) and 1395ww(d)(5), the Secretary was directed to impose, with certain exceptions, caps on DGME and IME FTEs using 1996 as the base year. The FTE caps are effective for IME for discharges on or after October 1, 1997 and for DGME for cost reporting periods on or after October 1, 1997. 42 C.F.R. §§412.105(f)(1)(iv) and 413.79(c)(2)(i).

There are two exceptions to the DGME and IME FTE caps that are pertinent to the instant case. The first exception permits a temporary adjustment to a hospital's FTE cap when that hospital takes on

[1] CMS re-designated the GME regulations from 42 C.F.R. §413.86 to 42 C.F.R. §§413.75 through 413.83 (69 FR 49254 (August 11, 2004)).

additional residents as a result of another hospital's closure. 42 C.F.R. §§ 412.105(f)(1)(ix) and 413.79(h)(1) and (2).

The second exception is an adjustment to a hospital's FTE cap resulting from the merger of two hospitals. 42 C.F.R. §413.79(e) (formerly 42 C.F.R. §413.86(g)(6)). The regulation does not specifically mention "merger;" however, in the preamble to the final rule, CMS advised:

> [W]hen there is a merger, the cap for the hospital should reflect the base year FTE counts for the hospitals that merged. This is consistent with the principle of limiting payments based on the base year specified in the statute. Also, in implementing the COBRA 1985 provision establishing a hospital-specific per resident amount in the situation of a merger, we have calculated the revised per resident amount for the merged hospital using an FTE weighted average of each of the respective hospital's per resident amount which is part of the merger. We believe that it would be appropriate to address the FTE caps using the same principle. For purposes of this final rule, *where two or more or more hospitals merge after each hospital's cost reporting period ending during FY 1996, the merged hospital's FTE cap will be an aggregation of the FTE cap for each hospital participating in the merger.* We are modifying § 413.86(g)(6) to reflect this change. (Emphasis added).

69 FR 26318, 26329 (May 12, 1998).

STATEMENT OF THE CASE AND PROCEDURAL HISTORY:

The Providers[2] comprising these group appeals are all affiliated with the University of Pittsburgh Medical Center (UPMC) Health System, an integrated healthcare delivery system of hospitals and physician clinics in Pittsburgh Pennsylvania. On August 19, 2002 UPMC entered into a transaction agreement with St. Francis Health System (SFHS) in which UPMC agreed to purchase from SFHS certain assets and accept the transfer of SFHS medical residents into its residency program.[3] On September 6, 2002 SFHS ceased operations and its Medicare provider number was terminated by CMS.[4]

For the cost report periods at issue, Highmark Medicare Services (formerly Veritus Medicare Services)[5] determined that since SFHS effectively closed its hospital, the Providers were entitled to temporary adjustments in their 1996 FTE cap amounts to account for the transferred SFHS residents. The Providers disagreed with the MAC's determination, maintaining that there was a constructive merger between UPMC and SFHS, and therefore there should be a permanent adjustment to their 1996 FTE cap amounts. The Providers timely filed a group appeal[6] with the Board and met the jurisdictional requirements of 42 C.F.R. §§405.1835-1841. The Providers were represented by Barbara Straub

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[2] See Appendix I for a listing of the Providers. Due to the common issues of law and facts in each case and for administrative efficiency, this decision combines case numbers 05-0508G, 06-0784G, 07-0510G, and 08-1412G. At the parties' request, case no. 08-1412G serves as the lead case in this appeal. *See*, Transcript (Tr.) at 18 and 19.

[3] Providers' Exhibit P-12.

[4] MAC's Exhibit I-16.

[5] In October 2007, as part of the Medicare Contract Reform, Highmark Medicare Services was awarded the Jurisdiction 12 Medicare Administrative Contractor (MAC).

[6] One Provider, Magee-Womens Hospital, initially filed an individual appeal, which was subsequently transferred to the group appeal by letter dated April 16, 2008. *See*, Provider's Exhibit P-1.

Williams, Esq. of Powers, Pyles, Sutter & Verville, PC. The MAC was represented by James R. Grimes, Esq. of BlueCross BlueShield Association.

STIPULATIONS:

The parties entered into a stipulation that sets forth the following factual findings:[7]

1. The issue in this case involves the "1996 resident cap," a Medicare program requirement that limits the number of full-time equivalent (FTE) residents that a hospital may count for purposes of direct graduate medical education (GME) and indirect graduate medical education (IME) payments to the number (sic) residents who were rotating at the hospital during the fiscal year that ended in calendar year 1996. More specifically, the issue is whether a *de facto* or constructive merger took place between University of Pittsburgh Medical Center (UPMC) Health System and St. Francis Health System (SFHS), thereby requiring an aggregation of the fiscal year 1996 resident caps for the UPMC Health System and SFHS providers under Medicare reimbursement policy. A tangential issue is whether, assuming that the transaction between UPMC Health System and SHFS (sic) is not a *de facto* merger, the Medicare policy that allows only a temporary adjustment to a hospital's 1996 resident cap when that hospital assumes the training for the residents displaced from a closed hospital is arbitrary, capricious, and an abuse of discretion.

2. For more than a century, SFHS, a nonprofit health care system, operated Medicare-certified acute care hospitals in the Pittsburgh area. Specifically, SFHS operated three inpatient acute care facilities: St Francis Medical Center (SFMC) in Lawrenceville, Pennsylvania, which was licensed for approximately 527 beds; St. Francis Hospital Cranberry ("St. Francis Cranberry"), which was licensed for approximately 35 beds; and St. Francis Hospital Newcastle ("St. Francis Newcastle"), which was licensed for approximately 142 beds.

3. In addition to its charitable healthcare mission, SFHS trained residents in GME programs.

4. Prior to the transaction at issue in this case, UPMC Health System and SFHS had partnered for several years on health care issues. In 1997, UPMC Health System and SFHS established a partnership to address the behavioral health needs of the Pittsburgh region through Community Care Behavioral Health Organization, a behavioral care management entity. In 1999, officials from UPMC Health System and SFHS held a series of meetings to discuss various options for collaboration between the two systems, including the creation of a Catholic division of UPMC Health System that would continue the SFHS's mission and purpose. In addition, UPMC Health System made a five million dollar charitable donation to St. Francis in September 2000 to assist it in continuing its health care and educational missions. UPMC Health System and SFHS also entered into an Affiliation and Management Services agreement that included various provisions for collaboration.

5. Minutes of the Board of Directors of UPMC (Exhibit P-9) indicate the Affiliation and Management Services Agreement included: the provision of management services by UPMC Health System to St. Francis Cranberry, the opportunity for UPMC Health System physicians to

[7] Stipulation of Parties, dated October 5, 2009.

obtain medical staff privileges at St. Francis Cranberry, the development of a joint study of the financial needs and potential opportunities at St. Francis New Castle, the offering of the UPMC health insurance plan to SFHS employees, the addition of the SFHS medical facilities to the UPMC health insurance plan network, the creation of a joint committee to consider and recommend further collaborative opportunities using new or existing resources, and the right of first refusal by UPMC Health System on the future disposition of SFHS programs and assets.

6. In the late 1990s, SFHS began to experience financial difficulties that continued through 2002. In early 2002, SFHS sent out a request for proposal seeking a partner organization that might help alleviate some of these pressures and further SFHS's charitable missions.

7. In May 2002, UPMC Health System and SFHS began negotiations for the sale of certain SFHS entities and assets. Jameson Health System, which operates an acute care hospital north of Pittsburgh, began negotiations with SFHS around the same time to purchase the assets of St. Francis New Castle.

8. UPMC Health System and SFHS entered into an agreement, dated August 19, 2002 (the "Transaction Agreement") to implement their purchase (Exhibit P-12).

9. Under the Transaction Agreement at §§ 21.1 [sic §§2.1] and 3.1, UPMC Health System agreed to pay $132 million for specified assets as described at § 2.2 of the Transaction Agreement of SFMC and St. Francis Cranberry, including all equipment and furnishing at those campuses.

10. The Transaction Agreement at §7.13 included a provision to transfer to UPMC Health System the types of residency programs previously operated by SFHS. This provision also stated that UPMC Health System would accept the transfer of the SFHS residents into its existing residency programs as long as the medical residents met its program requirements.

11. The Transaction Agreement at § 8.2 stated that only those certificates, licenses, permits or similar authorizations listed in Schedule 8.2 would be transferred to UPMC. Schedule 8.2 stated that the only "operating certificate" that SFHS was required to transfer to UPMC was "102 residents within St. Francis academic programs into UPMC teaching hospitals."

12. The Transaction Agreement at § 7.2 required SFHS to shut down its operation in accordance with a "Shutdown Plan." The Shutdown Plan required SFHS to cease providing all inpatient and outpatient clinical services and surrender all certificates, licenses, permits, and other authorizations with respect to its health care facilities, including SFMC and St. Francis Cranberry.

13. The Transaction Agreement at § 7.2(i) also required SFHS to terminate all contracts except certain contracts related to the operation of the SFHS facilities.

14. The Transaction Agreement at § 7.2(iii) required SFHS to terminate its employees, although UPMC Health System retained the right to hire those employees.

15. Under the Transaction Agreement at § 2.3, UPMC Health System accepted responsibility for liabilities associated with certain assets that it acquired. Specifically, UPMC Health System assumed liabilities relating to "Designated Contracts" continuing beyond the Shutdown period that had been held by SFHS with tenants and vendors (e.g. pest control, energy providers, elevator services). In addition, under § 2.3(c) and Schedule 2.3(c) of the Transaction Agreement, UPMC Health System assumed over $4.4 million in liabilities for accounts payable, mortgage payable, tenants' security deposits payable, and other liabilities.

16. Under the Transaction Agreement at §10.3(a), UPMC Health System agreed to use its reasonable efforts to offer positions to SFHS employees, including employed physicians, and agreed to recognize years of service with SFHS for purposes of determining salary, and wages and benefits for those employees.

17. UPMC Health System also agreed, under the Transaction Agreement at §10.3(d), to accept applications from SFHS physicians for appointment to the UPMC Health System medical staff, subject to meeting applicable requirements.

18. On August 20, 2002, SFHS petitioned the Orphans' Court Division of the Court of Common Pleas of Allegheny County, which has jurisdiction over the disposition of a nonprofit corporation's assets, to approve the Transaction Agreement between UPMC Health System and SFHS.

19. On September 27, 2002, the Orphans' Court approved the Transaction Agreement between UPMC Health System and SFHS. The Orphans' Court, which (sic) determined that the assets transferred to UPMC Health System were not being diverted to non-charitable uses and would continue to be used for a charitable purpose. Specifically, the Orphans' Court determined that, "UPMC is a reputable nonprofit charity that will further the mission and tradition of nonprofit health care in the region."

20. The Orphans' Court also approved an agreement to sell assets of St. Francis New Castle to Jameson Health System. Jameson Health System paid approximately $18 million for St. Francis New Castle.

21. The Orphans' Court appointed a receiver who paid all known liabilities of SFHS existing at the time from the $150 million total purchase price ($132 million paid by UPMC Health System plus $18 million paid by Jameson Health System). SFHS's liabilities at the time of the transaction were estimated to be $150 million.

22. Beginning August 20, 2002 (the day after SFHS announced the transaction with UPMC Health System to its staff), and continuing for two weeks afterward, UPMC Health System set up a job fair at SFMC to facilitate its hiring of SFHS employees. A similar, but shorter, job fair was held at St. Francis Cranberry.

23. UPMC Health System provided written materials to potential employees to explain the hiring process and credited SFHS employees with their years of employment at SFHS for purposes of obtaining benefits at UPMC Health System.

24. UPMC Health System also extended offers to SFHS medical staff to consider joining the medical staff of UPMC Health System.

25. UPMC Health System made offers to more than 800 SFHS staff, and 693 individuals accepted those offers. Approximately 94% of SFHS's behavioral workers chose to become employees of UPMC Health System. In addition, more than 400 of the 480 physicians on the SFHS medical staff joined the medical staff of UPMC Health System.

26. UPMC Health System and SFHS drafted a detailed plan for transferring SFHS's behavioral health patients to UPMC facilities. This plan also included provisions for UPMC Health System facilities to hire SFHS behavioral health employees and medical staff. UPMC continues to provide almost all of the behavioral health services that were previously provided by SFHS.

27. After the transaction between UPMC Health System and SFHS, UPMC's Children's Hospital opened on the site of the SFHS facility in Lawrenceville, Pennsylvania. UPMC Children's Hospital consists of some buildings constructed by UPMC and some SFHS buildings that were renovated by UPMC. St. Francis Cranberry terminated its Medicare Provider number, but continued to operate as a campus of UPMC Passavant Cranberry.

28. The change in population mix at UPMC Presbyterian and UPMC Shadyside[8] between 2001 and 2002 indicates that UPMC absorbed many of the elderly and indigent patient populations that SFHS had previously served. The chart below shows that the Medicare and Medicaid patient populations at UPMC Presbyterian and UPMC Shadyside increased at a much greater rate between 2001 and 2002 than did the overall patient population at the two hospitals.

UPMC Presbyterian and UPMC Shadyside Inpatient Admissions from SFMC Service Area						
	UPMC Presbyterian			**UPMC Shadyside**		
	Sept-Oct 2001	**Sept-Oct 2002**	**Increase**	**Sept- Oct 2001**	**Sept- Oct 2002**	**Increase**
All Patients	694	749	7.9%	728	1,203	65.2%
Medicare Total	367	418	13.9%	340	794	133.5%
Medicaid Total	103	135	31.1%	60	138	130.0%

29. The website for the Accreditation Council for Graduate Medical Education ("ACGME") shows that SFHS notified the ACGME that it was voluntarily withdrawing its Internal Medicine and Psychiatry residency programs on August 21, 2002 and its Radiology-Diagnostic residency program on September 1, 2002.

30. University Health Center of Pittsburgh informed the ACGME, by letter dated November 22, 2002, that it intended to accept all 88 displaced SFMC residents.

31. The Graduate Medical Education Directory (the "Green Book"), which is published by the ACGME and lists approved slots for residency programs, demonstrates that UPMC Health

[8] UPMC Shadyside and UPMC Presbyterian merged on May 31, 2003 to become UPMC Presbyterian Shadyside (one of the Providers in this case).

System obtained ACGME approval for assuming slots for residency programs previously training at SFMC. The chart below shows the number of slots in various residency programs at both UPMC Health System and SFMC in the 2000-01 academic year (i.e. before the transaction between UPMC Health System and SFHS) and at UPMC Health System alone in an academic year after the transaction.

Transition of SFMC Resident Slots						
Residency Program	SFMC Positions in Academic Year 2000-01	UPMC Positions in Academic Year 2000-01	Total	UPMC Positions after Transaction with SFHS	Difference	Provider Exhibit Reference
Diagnostic Radiology	15	28	43	42	<1>	P-16
Internal Medicine	33	109	142	145	3	P-17
Ophthalmology	6	15	21	20	<1>	P-18
Psychiatry	16	43	59	60	1	P-19

32. The Providers filed a "protested" affiliation agreement in each of its (sic) fiscal years 2003 through 2007 to show the claimed increase to the 1996 resident cap of the UPMC Health System flagship hospital, UPMC Presbyterian Shadyside, due to the assimilation of the SFHS residency programs, and how that 1996 resident cap is shared among the other hospitals in the UPMC Health System. The Intermediary did not accept the affiliation agreement because it contended that no affiliation of the programs was ever completed as required under (sic) Medicare Regulation.

33. The protested affiliation agreements were submitted to CMS and the Intermediary and otherwise met all procedural requirements related to Medicare affiliation agreements.

34. Neither the Medicare statute nor regulations define a merger for purposes of DGME and IME reimbursement.

35. UPMC and SFHS are Pennsylvania corporations. Generally, the laws of the state in which parties to a transaction are located govern the transaction.

36. The Providers train additional residents as a result of the St. Francis closing. However, the Providers' 1996 resident caps do not include the SFHS resident cap except for the temporary adjustment to the resident caps permitted under 42 C.F.R. §413.86(g)(8).

37. After the sale transaction between SFHS and UPMC, the Board of UPMC was not reconstituted, and no former SFHS Board members were given seats on the UPMC Board.

PARTIES' CONTENTIONS:

The Providers contend that UPMC Health System and SFHS underwent a *de facto* merger, and therefore

their 1996 FTE resident caps should be increased to include SFHS' 1996 resident cap.[9]

As stipulated by the parties, neither the Medicare statute nor the regulations define a merger for purposes of DGME and IME reimbursement.[10] As such, the Providers contend the laws of the state, in this case Pennsylvania, are to be applied in evaluating whether the transaction in this appeal was indeed a merger.[11] The Providers advised that Pennsylvania courts recognize the "*de facto* merger" doctrine, in which a transaction between two or more corporations has the effect of a corporate merger, despite the fact that the parties may not have called the transaction a merger or followed state regulatory requirements applicable to mergers.[12] The Providers advise that Pennsylvania courts look to the realities of a transaction rather than the corporate formalities to determine if a *de facto* merger has occurred. The Providers assert that the Pennsylvania courts have held that a *de facto* merger is evidenced by:[13]

1. Continuity of ownership;
2. A cessation of ordinary business and dissolution of the predecessor as soon as practically and legally possible;
3. Assumption by the successor of the obligations ordinarily necessary for the uninterrupted continuation of the normal business operations of the predecessor; and/or
4. A continuity of management, personnel, physical location, assets and general business operations.

The Providers contend that, after consideration of the above, the transaction between UPMC Health System and SFHS contains almost all of the most significant factors that the courts have determined are indicative of a *de facto* merger. First, the Providers argue there was a continuity of ownership between SFHS and UPMC.[14] The Providers advised that SFHS agreed to cooperate with UPMC because UPMC is a nonprofit corporation and shares its charitable health care mission. The Orphans' Court, which approved the transaction, also determined that UPMC Health System would further SFHS's mission and tradition of nonprofit health care.[15] Next, UPMC agreed to make its facilities reasonably available to SFHS patients after the closing date of the transaction.[16] Additionally, UPMC continued to operate SFMC as an acute care facility, but with a focus on pediatric care, after undertaking significant renovations of the SFMC facility to convert it to pediatric use.[17]

Second, the Providers contend that SFHS's cessation as a health care provider is indicative that a de facto merger occurred between UPMC and SFHS. The Providers assert that the Transaction Agreement required SFHS to shut down its operations in accordance with a "Shutdown Plan" and also required SFHS to terminate all contracts, except certain contracts related to the operations of the SFHS facilities.[18] The only "operating certificate" that SFHS was required to transfer to UPMC related to the continued operation of its residency programs. In addition, the Transaction Agreement required SFHS

[9] Providers' Position Paper at 14; Tr. at 11.
[10] Stipulation No. 34.
[11] Stipulation No. 35.
[12] Providers' Position Paper at 11.
[13] Providers' Position Paper at 13.
[14] Providers' Position Paper at 18.
[15] Providers' Exhibit P-14 at 267-68, §§6 and 7.
[16] Providers' Exhibit P-12, at 86, §§7.10 and 7.11.
[17] Providers' Exhibit P-11.
[18] Providers' Exhibit P-12 at 82, §7.2.

to terminate its employees, although UPMC Health System retained the right to hire those employees. Collectively, the Providers maintain that SFHS's corporate identity was permanently altered and essentially subsumed in the transaction with UPMC Health System, which is indicative of a *de facto* merger.

Third, the Providers contend that UPMC Health System assumed all of the obligations necessary to continue the services that SFHS previously provided.[19] Specifically, UPMC and Jameson purchased SFHS for $150 million, which was estimated to be SFHS's debt.[20] Therefore, the purchase price was sufficient to extinguish all of SFHS's existing liabilities. In addition, UPMC assumed over $4.4 million in liabilities for accounts payable, mortgage payable, tenants' security deposits payable, and other liabilities.[21] The Providers acknowledge that SFHS retained some liabilities, such as liability for certain past legal violations and malpractice liabilities; however, the retention of such liabilities can hardly be considered necessary for the uninterrupted continuation of normal business operations. The Providers assert that UPMC assumed practically all of SFHS's liabilities necessary for the uninterrupted continuation of SFHS's healthcare services.

Finally, the Providers contend that UPMC Health System's continuity of SFHS' management, personnel, physical location, assets and general business operations is indicative of a *de facto* merger.[22] As to the continuity of SFHS's management and personnel staff, the Providers' witness, Ms. Trott, testified that certain members of SFHS management team and other staff members continued those roles or similar ones at UPMC.[23] Additionally, out of 800 SFHS employees, 693 accepted job offers from UPMC and 400 out of 480 SFHS physicians accepted job offers at UPMC.[24] As to the continuity of SFHS's physical location, UPMC's Children's Hospital opened on the SFMC site, using some SFHS buildings that were renovated by UPMC.[25] Moreover, with the exception of specified religious articles, UPMC acquired all of the assets from SFMC and St. Francis Cranberry.[26] Furthermore, with regard to general business operations, the Providers assert that UPMC continued to provide the same health care services formerly furnished by SFHS including the operation of its medical residency training programs.[27]

The Providers also contend that CMS policy allowing only a temporary adjustment to a hospital's 1996 FTE resident cap when accepting residents from a closed hospital is arbitrary, capricious and an abuse of discretion.[28] The Providers acknowledge that the Board does not have jurisdiction to rule whether CMS policies are arbitrary and capricious, and have essentially reserved this issue for appeal to the federal courts.[29]

The MAC contends that the transaction between UPMC and SFHS was neither a statutory nor a *de facto*

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[19] Providers' Position Paper at 16.
[20] Stipulation No. 21.
[21] Stipulation No. 15.
[22] Providers' Position Paper at 17 -19.
[23] Tr. at 37-39, 52-55.
[24] Stipulation No. 25,
[25] Stipulation No. 27.
[26] Stipulation No. 9, Providers' Exhibit P-12 at 11-12, §§2.2 and 2.4.
[27] Stipulation No. 36; Tr. at 67-68, 74, 88 and 121.
[28] Providers' Position Paper at 21-26.
[29] Tr. at 134.

merger, and instead was simply an asset purchase, primarily involving the sale of land on which SFMC was located.[30] The MAC asserts there was no continuity of ownership of SFHS by UPMC Health System. Indeed, in its petition seeking approval of the sale before the Orphans' Court, SFHS acknowledged that there were no bids submitted that would have continued SFMC as an operating entity, and that UPMC Health System required that SFMC be closed so that a new Children's Hospital could be constructed on the site.[31]

Next, the MAC asserts that SFHS's cessation as a corporate entity was attributed to SFHS's severe financial difficulties and unrelated to the transaction with UPMC Health System.[32] The MAC maintains that SFHS had opted to close its operations prior to any transaction with UPMC.

The MAC contends that UPMC assumed liabilities related only to the purchase of SFHS' real estate and upkeep of the building, and declined to accept responsibility for any of SFHS' other liabilities, such as liabilities associated with its pension benefits and Medicare and Medicaid claims.[33] The MAC argued that under Pennsylvania law a merger results in a single surviving corporation, and all debts shall be deemed vested in and shall belong to the surviving corporation.[34] The MAC contends that UPMC's refusal to assume all of SFHS liabilities is a strong indication that a *de facto* merger did not occur.

As a final point, the MAC asserts that there was no continuity of SFHS's management, personnel, physical plant or business operations following the transaction. The MAC acknowledged that UPMC extended job offers to some of SFHS employees; however, no SFHS Board members were given seats on the UPMC board.[35] Additionally, UPMC did not maintain the SFHS hospital building, and instead constructed a new Children's Hospital at the site, which opened seven years following the purchase of the property.[36] The MAC contends that UPMC's construction of a new hospital several years after the transaction clearly shows a lack of continuity in SFHS' business operations. The MAC asserts that the transaction between UPMC and SFHS does not qualify as a *de facto* merger under Pennsylvania laws, and instead amounts to an asset purchase.

FINDINGS OF FACT, CONCLUSIONS OF LAW AND DISCUSSION:

After consideration of the Medicare law, regulations, and guidelines, the parties' contentions, and evidence presented, the Board finds and concludes that the transaction between SFHS and UPMC Health System was not a *de facto* merger. Therefore, the MAC's adjustment of the Providers' 1996 base year cap for purposes of DGME and IME payments was proper.

The Medicare statute at 42 U.S.C. §§1395ww(h)(4)(F) and 1395ww(d)(5)(B)(v) and the implementing regulations at 42 C.F.R. §§413.79(c)(2)(i) and 412.105(f)((1)(iv) provide for a cap, referred to as the "1996 resident cap," on the number of FTE residents for purposes of DGME and IME reimbursement. Although the law and regulations do not address application of the resident cap for hospital mergers, in the preamble to the final rule, CMS advised that when two or more hospitals merge, the merged

[30] Tr. at 24-25.
[31] Providers' Exhibit P-13 at 247, §§ 28 and 29; Tr. at 26.
[32] MAC's Position Paper at 6.
[33] MAC's Position Paper at 7; Providers' Exhibit P-12 at 12 §§2.4 and 2.5; Tr. at 91-101.
[34] 15 Pa. Cons. Stat. Ann. § 1929(b) (August 21, 2001). (contained in MAC's Exhibit I-9).
[35] Stipulation No. 37.
[36] MAC's Exhibit I-20;Tr. at 26,

hospital's FTE cap will be an aggregation of the FTE cap for each hospital participating in the merger.[37] The regulations do not define a "merger" for purposes of DGME and IME reimbursement; however other regulatory provisions refer to a statutory merger, as "a combination of two or more corporations under the corporation laws of the State, with one of the corporations surviving."[38] It is undisputed that no statutory merger, as defined under Pennsylvania law, occurred in the instant case.[39] Therefore, there is no explicit authority for combining FTE caps.

The Providers assert that Pennsylvania law describes a merger between corporations as one which results in a surviving corporation that succeeds to the assets and liabilities of the merged corporation.[40] The Providers urge the Board to recognize a *de facto* merger, as do Pennsylvania courts: only when a transaction between two or more corporations that has the effect of a statutory mergers it deemed to be a merger.[41] Accepting at face value the Providers' characterizations of what Pennsylvania case law establishes as the criteria for *de facto* mergers, the Board finds that the criteria was not met in the instant case.

Based on cases cited, the Providers acknowledge that the common principle underlying each court's inquiry is "whether the transaction had the same effect on the parties as a merger."[42] As described under Pennsylvania law, the hallmark of a merger is the absorption of the merged entity by the survivor corporation, including all its assets and liabilities and future and contingent obligations.[43] By contrast, an asset purchase permits limitation of liabilities to only those specifically acquired by the purchase.

The evidence shows UPMC was acutely aware of the distinctions between the types of transactions, as evidenced by the various forms of acquisitions it used in other transactions. For example, Ms. Trott, witness for the Providers, testified that UPMC had been involved in other types of transactions, including asset acquisitions, joint ventures, and stock ownership.[44] The evidence also shows that the transaction between UPMC Presbyterian and UPMC Shadyside was clearly defined as a merger.[45] Considering these facts, it is apparent that UPMC deliberately chose an asset purchase and the benefits associated with it in its negotiations with SFHS.

The record also shows UPMC Health System refused to assume all of SFHS' liabilities and obligations. As stipulated by the parties, UPMC's assumption of liabilities was limited to the real property it purchased from SFHS.[46] The Providers' witness was emphatic that UPMC Health System had no intention or expectation of assuming all SFHS liabilities, especially the pension obligations.[47] Although UPMC and Jameson paid funds estimated to be sufficient to liquidate those liabilities, it was SFHS, not UPMC that was left with the obligation to negotiate the pension settlements. Additionally, the

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[37] 69 Fed. Reg. 26318, 26329 (May 12, 1998).
[38] 42 C.F.R. § 413.134(k)(2) refers to statutory merger for purposes of valuation of assets for depreciation. 42 C.F.R. § 489.18(a) also refers to statutory merger for purposes of change of ownership.
[39] Tr . 21.
[40] Provider Position Paper at 10
[41] *Id* at 11.
[42] *Id* at 13.
[43] 15 Pa. Cons. Stat. Ann. § 1929(a) and (b) (August 21, 2001).
[44] Tr. at 103-104.
[45] MAC's Exhibit I-25 at 7.
[46] *See*, Stipulation No. 15.
[47] Tr. at 94 and 114-115.

transaction agreement lists a host of liabilities retained by SFHS, including, but not limited to: federal, state and local taxes, employee health and welfare benefit plans, employment discrimination claims, unemployment claims, workers' compensation claims, professional liability and general liability claims, and third party payor claims including payments made by Medicare, Medicaid and managed care organizations.[48] Moreover, the Orphans' Court order clearly provides for SFHS, and not UPMC, to liquidate the liabilities.[49]

The evidence also reveals that UPMC did not subsume SFHS's corporate identity. Central to SFHS's corporate identity was its three acute care hospitals in the Pittsburgh area, which consisted of SFMC with 527 beds, St. Francis Cranberry with 35 beds and St. Francis Newcastle with 142 beds. A review of the transaction agreement shows UPMC and Jameson essentially divided up SFHS, with each taking the pieces it wanted. UPMC bought the closed SFMC and St. Francis Cranberry, while Jameson acquired the second largest SFHS hospital, St. Francis Newcastle. SFHS kept other items, generally described as religious artifacts. The carving out of a major part of the assets for Jameson, in itself, indicates a failure to acquire substantially all the assets or to absorb the SFHS corporate entity into UPMC. Moreover, SFHS continued to exist as a corporate entity and continued business, albeit winding down, until at least 2006.[50]

The evidence further shows UPMC did not assume obligations ordinarily necessary for the uninterrupted continuation of the normal business operations of the predecessor, nor was there continuity of physical location, assets and general business operations of SFHS. On the contrary, UPMC continued to operate only the St. Francis Cranberry site. In partnership with Highmark, UPMC renovated and built new buildings on the former SFMC site to create a new pediatric facility that also offered an insurance option. In other words, UPMC used that portion of the SFHS real estate and, with its major construction project and insurance partner, Highmark,[51] offered an entirely new product. The evidence shows an increase in inpatient admissions after the transaction at UMPC. However this appears to be a natural repercussion of closing a major hospital in the same community, i.e., the competitor increased its market share because of the closure and discontinuation of SFHS' business operations.

The Board concludes that the transaction between UPMC and SFHS did not have the same effect as a merger and the *de facto* merger doctrine, even assuming it is available, does not apply in the instant case. Instead, the transaction involved an asset purchase. There is no legal authority that allows this type of a transaction to justify a permanent increase in a provider's 1996 resident cap.

Though UPMC may have in fact absorbed the SFHS graduate medical education programs, the increase was related to the closure of SFHS.[52] The regulations at 42 C.F.R. § 413.79(h) allow for the temporary adjustment to the resident cap due to a hospital closure. Accordingly, the MAC's adjustments to the Providers' 1996 resident caps for purposes of DGME and IME payments were proper.

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[48] Providers' Exhibit P-12 at 63-65, §2.5.
[49] Providers' Exhibit P-13 at 252-253.
[50] MAC's Exhibit I-20.
[51] Highmark's role in the transaction was not described during the hearing. *See,* Tr. at 106-07 and Providers' Exhibit P-6. However, the Provider's Exhibit P-13 at 8-10 provides some explanation of Highmark's involvement in the transaction. It appears the transaction was primarily between UPMC and Highmark to purchase SFMC.
[52] Stipulation No. 36.

Finally, the Board notes the Providers' contention that CMS's policy allowing only a temporary adjustment to a hospital's 1996 resident cap for the residents displaced from a closed hospital is arbitrary, capricious, and an abuse of discretion. As acknowledged by the Providers, the Board lacks the authority to rule whether CMS policies are arbitrary and capricious.

DECISION AND ORDER

The MAC properly calculated the Providers' 1996 resident caps for purposes of DGME and IME payments. The MAC's adjustments are affirmed.

Board Members Participating:

Suzanne Cochran, Esquire
Yvette C. Hayes
Keith E. Braganza, C.P.A.
John Gary Bowers, C.P.A.

FOR THE BOARD:

Suzanne Cochran, Esq.
Chairperson

DATE: October 28, 2010

APPENDIX I

Provider Number	Provider Name
39-3302	Children's Hospital of Pittsburgh Pittsburgh, Allegheny, PA
39-0178	UPMC Horizon Greenville, Mercer, PA
39-0114	Magee-Womens Hospital of UPMC Pittsburgh, Allegheny, PA
39-0002	UPMC McKeesport McKeesport, Allegheny, PA
39-0164	UPMC Presbyterian Shadyside Pittsburgh, Allegheny, PA
39-0102	UPMC St. Margaret Pittsburgh, Allegheny, PA
39-0131	UPMC South Side Pittsburgh, Allegheny, PA