With Prestige Comes Scrutiny

Directors and officers of nonprofit hospitals must understand their lofty responsibilities

By Leonardo M. Tamburello

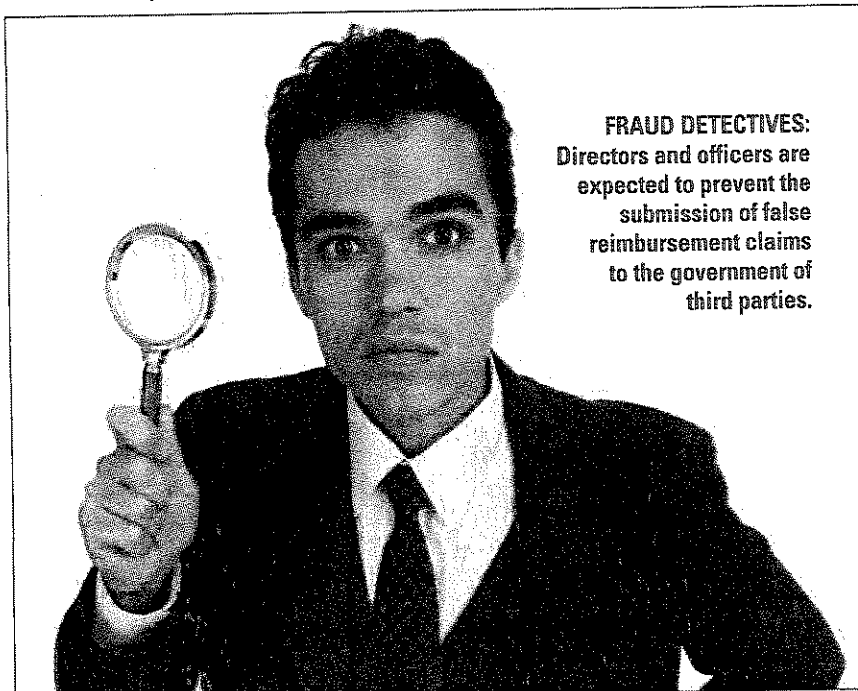
Directors and officers of nonprofit hospitals face challenges different from their counterparts in ordinary corporations due to the institution's position of public trust and the fact that a majority of the reimbursement comes from either the federal government through Medicare or Medicaid, or through private insurers. As a consequence of these funding sources, nonprofit directors and hospitals must consider the possible exposure of the institution and themselves to liability under the federal False Claims Act (FCA) 31 U.S.C. § 3729 et seq., and the New Jersey Insurance Fraud Prevention Act (IFPA) N.J.S.A. 17:33A-1 to -30.

Nonprofit hospitals are unique corporate creatures. They are neither governmental institutions nor private corporations, yet share the characteristics of both. Like government institutions, they furnish services that are vital to the public good; they are substantially funded from public and charitable sources and their activities are highly regulated. *Zoneraich v. Overlook Hosp.*, 212 N.J. Super. 83, 90 (App. Div.), *certif. denied*, 107 N.J. 32 (1986). Yet, like private institutions, nonprofit hospitals are operated by a Chief Executive Officer, are managed by unelected directors and officers, employ a multitude of workers and have sophisticated and far-reaching financial relationships. Nonprofit hospitals do not exist for pecuniary gain, but "for the benefit of the public," and "in aid of service to the public." Instead of assets or products, nonprofit hospital directors and officers "manage quasi-public trusts." *Greisman v. Newcomb Hospital*, 40 N.J. 389, 403-404 (1963). This elevated institutional status raises the legal and ethical bar for their directors and officers.

In an ordinary business setting, a corporation's directors and officers are regarded as fiduciaries who are supposed to act in the best business interest of the company. *Francis v. United Jersey Bank*, 87 N.J. 15, 36 (1981). They are expected to fulfill their responsibilities in good faith, with the level of care which an ordinarily prudent person would exercise in like circumstances. This standard, known as the "duty of care," requires that an officer or director act in an informed manner, exercise sound judgment, *In re Caremark International, Inc., Derivative Litigation*, 698 A.2d 959, 968 (Del. Ch. 1996), and demonstrate reasonable supervision and control over the policies and practices of the corporation as a whole. In the context of a nonprofit hospital, this includes preventing the submission of false reimbursement claims to the government or third-party insurers.

The FCA applies to fraudulent acts affecting contracts or entitlement programs administered by the federal government. In the nonprofit hospital setting, this includes all funding received from Medicaid, Medicare and federal grant funds. FCA actions may be initiated by private plaintiffs, including present or former employees, commonly known as "whistleblowers."

The essence of a claim under the FCA is the knowing submission of a false or fraudulent claim that is paid or approved by the government or the use of a false statement or record to get a claim paid or approved. 31 U.S.C. § 3729(a)(2). This requires proof: (1) that the institution made, used (or caused to be made or used) a record or statement to get a claim against the United States paid or approved; (2) that the record or statement and the claim were "false or fraudulent"; and (3) that the record or statement and the claim were known to be false or fraudulent at the time of



FRAUD DETECTIVES: Directors and officers are expected to prevent the submission of false reimbursement claims to the government of third parties.

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bring an action for IFPA violations. A person or practitioner violates the IFPA if they:

> [p]resents or causes to be presented any written or oral statement as part, or in support to, a claim for payment or other benefit pursuant to an insurance policy ... knowing that the statement contains any false or misleading information concerning any fact or thing material to the claim. N.J.S.A. 17:33A-4(a)(1).

A payer bringing suit under the act may seek compensatory damages, costs of investigation, costs of suit and counsel fees. Compensatory damages under the act may include all payments previously made to the provider. *Material Damage Adjustment Corporation v. Open MRI of Fairview*, 352 N.J. Super. 216, 232 (Law Div. 2002). Treble damages are also available "if the court determines that the defendant has engaged in a pattern of violating the act." A "pattern" is defined as "five or more related violations under [the Act.] Violations are related if they involve either the same victim or the same or similar actions on the part of the person or practitioner charged with violating [the act.]" A violation of the act can be proved by a preponderance of the evidence; the more stringent standard of "clear and convincing" found in common-law fraud is not needed. *Liberty Mutual v. Land*, 186 N.J. 163, 165 (2006).

Under both the FCA and the IFPA, a prevailing plaintiff may also recover treble punitive damages and counsel fees. N.J.S.A. 17:33A-7; 31 U.S.C. § 3730(g). The FCA also allows a successful plaintiff to share in a percentage of the government's recovery, while the IFPA raises the possibility of civil monetary penalties payable to the Office of the Insurance Fraud Prosecutor. N.J.S.A. 17:33A-5; 31 U.S.C. § 3730(d). In either case, the matter may be referred to law enforcement for possible criminal action against the institution, its representatives, or both.

Because of the quasi-public trust status of nonprofit hospitals, these institutions and their officers and directors receive greater public attention and scrutiny than ordinary corporations. An adverse FCA or IFPA determination against a nonprofit hospital has potentially far-reaching consequences beyond the hefty fines and penalties. Public perception as to the institution's overall adequacy to serve its patients can be eroded, and because of this, physicians may elect to admit their patients at competing institutions. Equally significant, fundraising and other foundation-type events may be adversely impacted.

An institution facing suspected FCA or IFPA violations is best served by officers who promptly investigate the situation. The first step should include preservation of the evidence in its original, untainted format. Following this, the board should appoint an independent committee to fully investigate the matter and report to the full board, less any members who are obviously conflicted from considering the matter.

If this internal investigation reveals a likelihood that a fraudulent practice has occurred, counsel should be immediately retained to assess whether the FCA or IFPA is implicated and decide on an immediate course of corrective action. Even if no impropriety is revealed, the fact that an investigation has taken place, its methodology and outcome should also be documented and made part of the facility's institutional knowledge.

In all circumstances, nonprofit officers and directors must be mindful and vigilant regarding their unique role as not only corporate officers, but as representatives of an institution which is a quasi-public trust. Nonprofit officers and directors should be aware that with this prestige also comes greater responsibility. ■