

OPPORTUNITIES AND PITFALLS IN HEALTHCARE PARTNERSHIPS WITH FEDERAL AGENCIES

Karen D. Powell, Esq.
Joseph J. Petrillo, Esq.

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The outlook is brightening for companies which sell health care services and resources to Federal agencies. Ongoing reorganization of major delivery systems provides new prospects. Moreover, much of the new business will be contracted on a local basis, which should open up the Federal market to new players. Provider-Sponsored Organization, for instance, might benefit in particular. However, as with any Federal contract, health care contracts can present unique pitfalls for the contractor, especially an inexperienced one.

The Landscape

The Federal Government is both the largest consumer and the largest domestic provider of health care services. Government-owned or operated medical facilities service more than 25 million Americans. The Veterans Health Administration, Bureau of Prisons and Public Health Service all have major programs, but the Department of Defense, directly and indirectly serving 8.2 million individuals, is the largest player. DoD is responsible, not only for active-duty personnel, but also for military dependents and retirees (to age 65) through the CHAMPUS program. DoD's multi-billion dollar budget pays for a direct-care system including 115 hospitals and 470 associated clinics, generically called Military Treatment Facilities ("MTFs"). DoD meets its obligations to CHAMPUS participants through the MTFs, through reimbursement to private providers, and now through regional contractors.

Most Government facilities augment their in-house resources with help from contracted sources. Contractors not only provide supplies and ancillary support, they can supply complete medical departments, such as radiology or ER, or provide individual physicians and nurses as needed. Again, DoD awards most of these contracts, to supplement its own direct care network. Recent policy changes will probably increase DoD contracting in this area.

DoD — The Biggest Customer Gets Bigger

This year, two initiatives will empower MTF Commanders, and increase their incentives to form beneficial partnerships with the private sector. One is a move to a capitation system for funding MTFs. The other, called Medicare subvention, directs additional funding to MTFs when they provide health care to Medicare-eligible retirees.

These initiatives may reverse a recent trend in DoD towards dependence on large, regional contracts for CHAMPUS health care. DoD is almost finished with establishing a nationwide system of seven huge regional contracts, held by a handful of large concerns. These contractors will provide all CHAMPUS care not furnished by MTFs.

In addition, the regional contracts include a "resource support" feature, under which MTF's, through a regional "Lead Agent," could order up to a specified dollar limit of medical capabilities from the contractor. Most regional contractors have teamed with a single provider for all such orders, so subcontracting opportunities have been scarce. But resource support hasn't met DoD cost-savings projections, and a 1996

GAO study concluded that it probably wouldn't. The stage was set for a new approach.

MTFs Become Businesses.

The first initiative — Enrollment Based Capitation ("EBC") — is a bold program to have military health administrators think like their private-sector counterparts. Starting in fiscal 1998, MTF budgets will depend, in part, on the size of enrolled populations. By fiscal 1999, the funding for an individual MTF will be adjusted by a formula assessing utilization, enrollment, and the size of the eligible population.

Like all capitation plans, the EBC program encourages the MTF to maximize efficiencies. Since most MTFs are large, established facilities, they need to maintain volume to be economically viable. Therefore, MTFs now have an incentive to retain or recapture CHAMPUS beneficiaries who might look to the regional CHAMPUS contractor for care.

The second program addresses an anomaly in the CHAMPUS system. Retirees aged 65 or older can't get reimbursement from CHAMPUS, and must look instead to Medicare. However, they still can get care from MTFs on a space-available basis.

A Medicare subvention demonstration project enables MTFs to get some reimbursement for care to senior citizens. Under this program, called TRICARE Senior, MTFs can enroll and service CHAMPUS eligibles over 65. Medicare then pays the MTF 95% of the local HMO reimbursement rate for each enrollee. So far the pilot only affects six sites. If the program becomes full-scale it too is likely to increase contracting opportunities. MTFs will want to round out their capabilities to attract more enrollees in TRICARE Senior, and contracts are the quickest way to do this.

The new initiatives put more authority and money in the hands of local MTF Commanders, which makes contracting on a local basis more likely. At a minimum, the regional CHAMPUS contractors might have to face competition for resource support business.

Avoiding the Pitfalls.

Like all Federal contracts, however, partnership agreements with MTFs have their own unique risks and requirements. Court decisions suggest some pitfalls. The problems encountered show that both the MTFs and contracted health care providers are new to contracting and haven't yet learned important fundamentals.

Nothing Casual About It

One problem in Government contracting is making sure that you are dealing with someone who has the requisite authority to commit the Government. This can sometimes be a challenge, since contracting power has bounced among MTF Commanders, Lead Agents, the central CHAMPUS office, and the Office of the Assistant Secretary of Defense.

One unfortunate contractor, providing pediatric services at an MTF, was directed by on-site personnel to have its x-ray technician support military physicians. When the contractor sought additional payment for the associated costs, however, it learned that those who had ordered the extra work lacked authority to do so. Even the courts were powerless to compensate the contractor for its extra work.

The Hidden Contract Term.

Experienced Government contractors know that the "contract" consists of more than a pile of signed papers. It is supplemented by a variety of regulations, including required contract clauses which may not

even be physically present in the formal documents.

In a recent court case, a contract for internal medicine services ran into this problem. The contractor had the good sense (or good fortune) to deal with authorized Government officials. However, the contract terms permitted payment at a rate higher than that prescribed by published regulations. The Government escaped liability for the higher rates. The court held that the contractor was charged with knowledge of the regulation, and should have known that its contract was illegal.

Beside the CHAMPUS regulations, there are restrictions on allowable charges found in the Medicare regulations, limitations on the amount the Government may be charged for pharmaceuticals under both HHS and VA regulations, and even limitations imposed by Government cost principles contained in the Federal Acquisition Regulations can have an impact. A contractor must beware.

Just because you can't do it . . .

The problems with illegality don't always affect the Government as strictly as the contractor. In an interesting case involving the Veteran's Administration, a losing contractor protested an award, charging that a feature of the contract was an kickback in violation of the Social Security Act. The General Accounting Office, which heard the protest, dodged the issue. It said that such matters were the responsibility of another Federal agency, HHS.

A Word to the Wise

Those seeking to capitalize on new contracting opportunities need to take care. The contents of the agreement should be at least as carefully drafted as a contract with a private-sector concern. Further, the contractor needs to consider that Government contracts and health care are both heavily regulated activities. It would be prudent to have qualified legal counsel participate in the negotiation and review of such agreements. If adequate precautions are taken, the rewards can outpace the risks.