AMERICAN BANKRUPTCY INSTITUTE
JOURNAL
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Intensive Care

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Federal and State Oversight of SNFs

What Happens at the Point of Enforcement?

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The health care industry is one of the most heavily regulated industries in the U.S., with multiple layers of oversight at the federal, state and local levels. Both federal and state agencies have various statutory powers to wield in order to ensure the health, safety and well being of patients in the U.S. health care system. At the most granular level, medical professionals are subject to continuing medical education requirements and standards of care for continuation of their medical licenses. The same is true for nursing homes and other providers. The federal government, through the Centers for Medicare and Medicaid Services (CMS), and the state government, through their departments of health (DOHs), regularly inspect and review skilled nursing facilities (hereinafter, "the survey process").

If a skilled nursing facility (SNF) fails to maintain minimum quality-of-care metrics and has survey deficiencies, the SNF might be assessed fines or penalties, or be subject to a plan of correction. In more serious instances, a state monitor might be put in place at the expense of the facility; the facility might then be deemed a special-focus facility, which can have a devastating impact on census and cash flow; and ultimately, the facility can lose its license and provider numbers, resulting in a loss of Medicare and Medicaid reimbursements. If an SNF loses its provider numbers and can no longer receive Medicare and Medicaid reimbursements, it will be completely dependent on private pay. Given that private pay patients comprise an immaterial component of the typical SNF's revenue stream, the termination of governmental and commercial payor contracts is the death knell for any SNF. If the regulators commence an administrative-hearing process to terminate an SNF's license and participation in the Medicare and Medicaid programs, what happens next?

This article begins with an overview of the federal and state regulatory process leading to an SNF's license and provider numbers being in jeopardy. Next, it explores the options for an SNF facing these regulatory issues, including a brief discussion of whether bankruptcy is an option and whether a receiver can be put in place by a lender or landlord to protect the SNF's license and provider numbers. The article concludes by discussing DOH receiverships when no other options are available, or when the state decides to step in and run the SNF.

Regulation and Enforcement Start at the State Level

Oversight, regulation and enforcement are generally at the state level and generally within the purview of the state's DOH. DOH typically assists CMS with certifying SNFs for participation in federal reimbursement programs, such as Medicare. DOH monitors facilities primarily through surveys, which are typically conducted annually and more frequently at facilities with more serious and/or unresolved deficiencies. A survey is usually conducted by a team consisting of a registered nurse with a social worker or nutritionist. At a very high level, the survey team will spend several days at the facility observing the care of the residents (medical and nursing care, meals, therapy, psychological support and social programs), and they will conduct a medical records review.

For a facility to reach the point of losing its license and Medicare and Medicaid provider numbers, a series of events will typically occur over time. In the event of a poor or failed survey outcome, DOH typically follows these steps:

- The SNF receives a letter notifying it of survey deficiencies, which will likely include an assessment of penalties and short time frame for correcting the deficiencies;

• If the SNF fails to correct the deficiencies, it will become subject to more acute oversight and more frequent surveys;
• If deficiencies persist unabated, the SNF will continue to be assessed penalties and the process for de-licensure might be commenced;
• Prior to terminating the license or commencing the process to de-license the SNF, DOH might take intermediate steps such as putting a state monitor or temporary manager in place to oversee resident care (at the expense of the facility), banning admissions and re-admissions, or issuing the facility a provisional license pending correction of the deficiencies;
• If the SNF cannot correct the deficiencies, the regulators will proceed with an administrative process to terminate the license and the provider numbers for Medicaid and Medicaid billing; and
• Once the administrative proceedings are completed, the SNF will be closed given that it is no longer licensed as an SNF (at this point, the state might need to step in to close down the SNF, including transferring residents to new facilities, disposing of medical waste and arranging for the storage of medical records — all of which takes time and costs money).

Bankruptcy and Receivership as an Option

A few SNFs have unsuccessfully attempted to use bankruptcy and the resulting automatic stay to prevent state and federal regulators from terminating licenses and provider numbers.[1] Generally, based on these recent cases, a bankruptcy filing likely will not prevent state and federal agencies from continuing or completing the administrative process to de-license a facility and terminate provider numbers. For a bankruptcy filing to be successful, at an early point in the failing-survey process the operator would need to file for bankruptcy, with the goal of closing a quick transaction to turn over the SNF to a new operator that has a good track record with regulators.

If the SNF has a working-capital lender or third-party landlord, it will sometimes be placed into receivership by the lender or landlord, with a third-party receiver appointed to oversee the SNF. This third-party receiver must work with the state regulators to correct any survey deficiencies and promptly transition the SNF to a new operator. As with a bankruptcy filing, the receivership process will not stop the enforcement actions of the federal and state agencies, but it might provide a forum to address the concerns of the regulators and preserve the SNF's value through a transition to a new operator.

For a lender dependent on being repaid from Medicaid receipts or a landlord dependent on maintenance of the license for asset-value preservation, the lender or landlord will be motivated to provide funding for the receivership, either directly or indirectly, and will be motivated to work with the regulators to ensure that the SNF's license and provider numbers are maintained. For the regulators, if a new operator is put in place and survey deficiencies are addressed by the receiver in the interim, the regulators will benefit from this outcome.

However, there are times when there is no lender or landlord willing to step in and support the SNF through a bankruptcy or receivership process aimed at addressing the deficiencies and transitioning the facilities to new operators. In this circumstance, the continuation of resident care at the site becomes a problem for the state.

DOH Receiverships

Under most state laws, a DOH can appoint a receiver and take over a facility in order to protect the well-being of the residents.[2] Most of the state statutes allowing a DOH to appoint a receiver or similar official are vague and do not have developed regulations or case law concerning their implementation. Generally, a DOH might commence a receivership against an SNF that has repeated failed surveys and is in the process of losing or has lost its license to operate.

In addition, if a facility is no longer able to operate due to financial constraints and does not have a lender or landlord willing to fund ongoing operations, the SNF might turn over operations to the DOH. While having a DOH step in to protect the residents seems logical, and a DOH might be well equipped to ensure the proper care and safety of residents, a DOH might not be equipped financially for the burden of operating or closing down an SNF. A DOH might have to support the SNF financially for months while a new operator is located or the facility is closed. For example, if the SNF's residents are at high-acuity levels with low reimbursement rates, it might be difficult to find facilities willing to admit

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1 *See Home Care Providers Inc. v. Hemmelgarn (In re Nightingale Home Healthcare Inc.)*, 861 F.3d 615 (7th Cir. 2017) (district court overturned bankruptcy's court injunction preventing government from terminating debtor's provider agreements; on appeal, district court decision was overturned given that at time of consideration, bankruptcy court had dissolved injunction and therefore district court should therefore have dismissed appeal as moot); *Florida Agency for Health Care Administration, et al. v. Bayou Shores SNF LLC (In re Bayou Shores SNF LLC)*, 828 F.3d 1297 (11th Cir. 2016) (bankruptcy court lacked jurisdiction to enjoin termination of debtor's provider agreements); *Parkview Adventist Med. Ctr. v. U.S.*, 842 F.3d 757 (1st Cir. 2016) (termination of provider agreements did not violate automatic stay or nondiscrimination provisions of Bankruptcy Code); *but see Sullivan v. Town & Country Home Nursing Servs. Inc. (In re Town & Country Home Nursing Servs. Inc.)*, 963 F.3d 1146 (9th Cir. 1992) (debtor's failure to exhaust administrative remedies did not deprive bankruptcy court of jurisdiction).

2 *See, e.g.*, MD Code, Health-General § 19-334 (2018) (secretary of health may petition for appointment of receiver for SNF after investigation if secretary determines that there is imminent danger of death or serious mental or physical harm to individuals at facility); M.S.A., Chapter 144A.15 (2017) (commissioner of health may petition district court in which facility is located for order directing commissioner of health to be appointed as receiver to operate facility); *McKinney's Public Law* § 2810, N.Y. Pub. Health § 2810 (2018) (owner of residential health care facility may request DOH to take over operations of SNF at any time by appointment of receiver; if operating certificate is revoked, commissioner may be appointed as receiver; receivership will terminate 18 months after commencement); 35 P.S. § 448.814 (2018) (DOH may appoint temporary manager of facility when provider is in violation of regulations); R.I. Gen. Laws § 23-17.11-6 (2018); (DOH may appoint receiver for SNF where it is determined that SNF is being mismanaged or improperly operated).

these challenging residents, and it is likely not permissible for an SNF to be closed until the last resident is transferred to comparable accommodations.

DOH receiverships are rare. For example, since 2009, the Minnesota DOH has been a nursing home receiver three times, affecting five SNFs.[3] While rare, on March 23, 2018, Nebraska's Department of Health and Human Services commenced a receivership against Cottonwood Healthcare, also known as Skyline, which operated 21 nursing homes and 10 assisted-living facilities across 19 counties in the state.[4] At the time of commencement of the receivership, Cottonwood Healthcare had 2,000 residents, 1,600 employees and three weeks of unpaid payroll, was unable to pay for supplies, and lacked sufficient funds to ensure the ongoing care of its residents.[5]

After the receiver was put in place, a Nebraska lawmaker noted that the state did the right thing, but highlighted the ongoing funding needs of Cottonwood Healthcare as a major issue for the state.[6] This lawmaker warned that with rising health care costs and an aging population, coupled with low Medicaid reimbursements rates, the Cottonwood Healthcare receivership might be one of many to come, resulting in a greater financial burden on the state.[7] According to reports, CMS is supposed to provide funding for the Cottonwood Healthcare facilities, if needed, in order to ensure the safety and well-being of residents.[8]

The Cottonwood Healthcare receivership highlights the many questions that typically arise as to how these DOH receiverships work in practice rather than theory. Here are some of the practical considerations.

Funding

As previously noted, one of the biggest concerns in any receivership is funding. Facilities that end up in a receivership typically have low census, low reimbursement rates and high costs. For a state-sponsored receivership, the state will need to access government funds to support the health care facilities until they are closed or transitioned to new operators, which will likely be a multi-month process. The facilities will likely not generate sufficient cash flow to cover the expenses of the receivership if they were unable to cover operating expenses prior to the commencement of the receivership.

In Minnesota, "During the receivership, an enhanced Medicaid rate is set ... to pay for the extra costs required during the receivership to get the facility back into compliance with laws, pay the employees, reinstate insurance and [pay] all other costs of operating a facility."[9] However, this enhanced reimbursement rate is not set until after commencement of the receivership and the managing agent, who operates the SNFs for a DOH, justifies the need for an enhanced reimbursement rate to the regulators.[10] Therefore, the benefit of this enhanced funding might be delayed and too late.

Employees

Do the employees of the SNF placed into receivership work for the receiver, the state (which commenced the receivership) or the operator? In receiverships commenced by a lender or landlord, the employees typically remain employed by the existing operator. In Minnesota, the DOH appoints a managing agent, who can terminate and hire employees only with the approval of the DOH, giving the state some control over employees — control that the state might not want.[11]

License-Holder/Regulation

Does the state, receiver or operator hold the license after the commencement of a receivership? Typically, the license continues to be held by the existing operator when a lender or landlord commences a receivership, and the receiver operates under that license. If a DOH commences the receivership and the facility is already de-licensed or in the process of losing its license, the state will presumably allow the receiver to operate the facility under some form of temporary or provisional license.

In Minnesota, if a receivership process has been commenced, the Minnesota DOH is the facility licensee, is issued a new license and appoints a managing agent to run the facility.[12] The former operator/licensee is no longer licensed.[13] In addition, given that the DOH commences the receivership, will the receiver benefit from relaxed federal and state regulations in an effort to effect a quick, efficient closure or transition of the SNF? In Minnesota, the DOH stresses that there are often "many serious health and safety violations at the facility and the managing agent is required to operate the facility in compliance with state and federal laws ... and must be able to correct the violations very quickly."[14] This statement suggests that the state's managing agent will be held to the same standards as any other operator holding a license in Minnesota.

Liability

If the state is viewed as running the SNF, then the state has potential liability to residents, employees and others. If there are wrongful-death claims or employee-related claims (for failure to pay wages, salaries, benefits or WARN claims) during the receivership, the state might have substantial exposure unless it can take advantage of sovereign immunity protections. For example, in Minnesota, a court can appoint the commissioner of the DOH as the receiver to take charge of an improperly run or financially distressed facility, and the commissioner will then enter into an agreement with a managing agent who operates the facility on the commissioner's behalf.[15] This type of arrangement, with the commissioner as the receiver, creates a much closer relationship between the state and the SNF, which might increase exposure to the

3 "Minnesota Department of Health Seeks Nursing Home Receivership Managing Agent Candidates," Minnesota Department of Health, *available at* health.state.mn.us/divs/fpc/receivership.html (unless otherwise specified, all links in this article were last visited on March 30, 2018).

4 Maggie Flynn, "Chain of 21 Nursing Homes Placed in Receivership," *Skilled Nursing News* (March 26, 2018), *available at* skillednursingnews.com/2018/03/chain-21-nursing-homes-placed-receivership.

5 *Id.*; *see also* Mike Loizzo, "Senator Warns of More Troubles After 21 Nursing Homes and Assisted Living Facilities Placed in Receivership," Nebraska Radio Network (March 26, 2018), *available at* nebraskaradionetwork.com/2018/03/26/senator-warns-of-more-troubles-after-21-nursing-homes-assisted-living-facilities-placed-in-receivership.

6 *Id.*

7 *Id.*

8 *Id.*

9 *See* Flynn, *supra*, n.4.

10 *Id.*

11 *Id.*

12 *Id.*

13 *Id.*

14 *Id.*

15 Minn. Stat. 144A.15, Subd. 2 (2017).

state from any resulting liabilities while the SNF is under their control.

Admissions

If the SNF is in the process of losing its license, the receiver might not be able to accept new admissions and might need to begin the process of transferring residents given that it will not be cost-effective to maintain the necessary staffing levels as the census drops. Declining staff, time to transfer residents and staff costs place further financial burdens on the SNF and the state.

Claims Adjudication/Wind-Down

Are the DOH and appointed receiver obligated to wind down the operator's business after the SNF is closed or transferred to another operator? Does the state have to fund the receiver to reconcile claims and pay out vendors, employees, and others? If required, this is yet another additional cost to the state.

Existing Leases and Contracts

If the SNF is closed or transitioned to a new operator as part of the receivership process, the receiver will continue to operate the SNF for some time while residents or operations are transferred. If the receiver operates under a new license, an issue will arise as to whether the receiver can continue to operate under existing leases and contracts. Moreover, if the receiver is a state agency, will that state agency have to go through a typical government contracting process to enter into new leases and contracts?

If the facility is leased, do the DOH and receiver have an obligation to fund monies to pay ongoing rental payments, deferred maintenance expenses and other costs to be incurred in cleaning up the facility before delivering possession to the landlord? This is a potential risk to the landlord, whose asset value might be depleted if these costs are not paid, and a potential significant cost to the state if the state must fund compliance with the lease.

What Does This Mean for a State?

There is no developed body of case law or regulations to address these issues in DOH receiverships. If a DOH commences a receivership against one or more SNFs, the state is potentially obligated for substantial expenses and liabilities that will not be funded by the SNF's ongoing cash flow. With many states already in financial distress, any additional financial burden, such the financial burden of running troubled SNFs, will only add to states' problems.

Conclusion

Given the extensive regulation of the health care industry, the low reimbursement rates for SNFs, the often slow pay by certain states for Medicaid reimbursements and the declining census at SNFs due to recent trends to move residents to a lower-cost setting of care (*i.e.*, home through Medicaid waiver programs), the financial pressures on SNFs will continue to increase. As this occurs, states might be asked or forced to take over SNFs as they fail financially, if there is no prospect of a new operator taking over the facility in the short term.

As states take over SNFs and likely commence receiverships to do so, they will need to address these issues — most importantly, how to finance the costs of either running or shutting down these facilities. The *Cottonwood Healthcare* receivership will be a good case study as to how a state manages the process of operating large facilities with more than 2,000 residents and 1,600 employees. abi

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