



**Buchanan
Ingersoll &
Rooney** PC

Limiting Your Liability:

How Healthcare Providers Can Defend Against Piercing the Corporate Veil Claims

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The background features a collection of white line-art icons within hexagonal frames. These icons include a water drop, a clipboard, a first aid kit, a heart with an ECG line, a syringe, a DNA double helix, a flask with bubbles, and two test tubes. Additionally, there is a network diagram with nodes and connecting lines. The overall theme is medical and scientific.

Agenda

- Background: Corporate Negligence
- Overview: Piercing the Corporate Veil
- Case Studies
- Recent Developments
- Recommendations
- Questions

The background of the slide is a grayscale photograph of a medical setting. In the upper portion, an ECG (heart rate) monitor is visible, showing a regular rhythm with several heartbeats marked by small black dots. Below the monitor, a stethoscope is resting on a surface, with its chest piece and earpieces clearly visible. The overall scene is softly lit, creating a professional and clinical atmosphere.

Background: Corporate Negligence

History of Corporate Negligence in PA

- *Thompson v. Nason Hosp.*, 527 Pa. 330 (1991)
- Corporate negligence is a doctrine under which a hospital is liable if it fails to carry out the non-delegable duties it owes to patients.
- A hospital's duties are:
 1. use reasonable care in the maintenance of safe and adequate facilities
 2. select and retain only competent physicians
 3. oversee all persons who practice medicine within its walls
 4. formulate, adopt and enforce adequate rules and policies to ensure quality care for the patients

Scampone: Extended Corporate Negligence to Nursing Homes

- *Scampone v. Highland Park*, 57 A.3d 582 (2012)
- Extended corporate negligence doctrine in *Thompson* to skilled nursing facilities
- Required an individualized inquiry into the role of each entity to ensure that multiple entities are not exposed to liability for breach of the same non-delegable duties

Do corporate entities owe a duty to plaintiff?

Richard Scampone, as Executor of the Estate of Madeline Scampone

v.

Grane Healthcare Company, Grane Associates, L.P., Highland Park Care Center, LLC d/b/a Highland Park Care Center, & Trebro, Inc.

2017 Pa. Super. 257, 2017 WL 3392480 (Pa. Super. 2017)

Duty of Management Company

- August 8, 2017: Superior Court Finds Management Company Had a Duty to Ms. Scampone
 - Pursuant to the management services contract, “management company” created policies & procedures
 - Even though Highland Park set staffing levels, “management company” approved the budget
 - “Management company” hired & trained licensed operator’s registered nurses & appointed its Director of Nursing

Duty of Management Company

- “Management company” employed nurse consultants who visited licensed operator weekly to oversee patient care
- “Management company’s” employee supervised licensed operator’s Administrator
- “Management company” established & administered a Quality Assurance Program

Holding

- *Only* the licensed operator may be directly liable for corporate negligence
- “Management company’s” contractual undertaking to manage & oversee the resident’s care was necessary for her protection
- “Management company” may be vicariously liable for the actions of its nurse consultants, who oversaw the licensed operator’s staff & failed to ensure patients received appropriate care. But it has no direct liability.



Overview: Piercing the Corporate Veil

Incorporation

- A corporation is a legal entity that is **separate** and **distinct** from its owner(s)
- Enjoys most rights and responsibilities that individuals possess
 - Entering contracts
 - Loaning/borrowing funds
 - Sue and be sued
 - Hire employees
 - Own assets
 - Pay taxes

Incorporation (cont.)

- A corporation is created when it is incorporated by a group of shareholders who have ownership of the corporation, represented by their holding of common stock, to pursue a common goal
- The corporation is considered an **individual entity** under the laws of the state in which it was incorporated
- Functions through the acts of its directors, officers and employees, and is generally liable for such acts

Incorporation (cont.)

- Limited Liability Benefits
 - Shareholders, officers, directors and employees avoid personal liability for their negligent acts or omissions in carrying out their corporate duties
- General rule of limited liability **applies to CMS and its contractors** when dealing with shareholders of incorporated health care providers, just as it does to other creditors



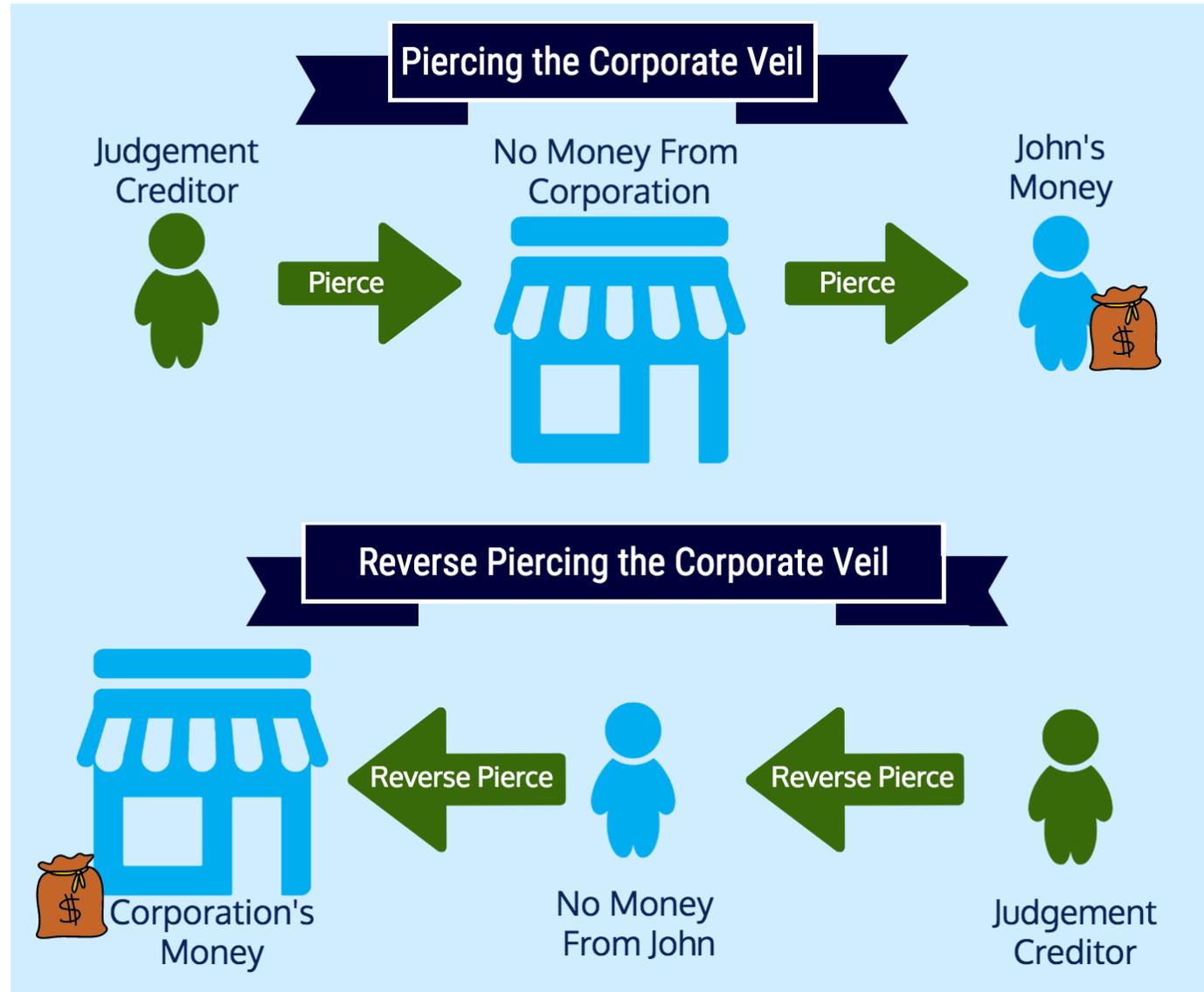
“The legal fiction that a corporation is a legal entity separate and distinct from its shareholders was designed to serve convenience and justice, and will be disregarded whenever justice or public policy require and where rights of innocent parties are not prejudiced nor the theory of the corporate entity rendered useless. We have said that whenever one in control of a corporation uses that control, or uses the corporate assets, to further his or her own personal interests, the fiction of the separate corporate identity may properly be disregarded.”



Ashley v. Ashley, 482 Pa. 228, 237, 393 A.2d 637, 641 (1978);

Barium Steel Corp. v. Wiley, 379 Pa. 38, 108 A.2d 336 (1954)(plurality)

“Piercing the Corporate Veil”



“Piercing the Corporate Veil:” Equitable Remedy

- Traditionally, courts have strongly presumed **against** piercing the corporate veil, doing so only if there has been serious misconduct.
- The party seeking to pierce the corporate veil must establish that the owners, through their domination, abused the privilege of doing business in the corporation form to “**perpetrate a wrong or injustice against that party such that a court will intervene**”
- As an equitable remedy, plaintiffs must assert an **underlying claim, inequitable result** in order to pierce the veil
 - *i.e.*, breach of contract, negligence, fraud, breach of duty, siphoned funds, insolvency

“Piercing the Corporate Veil:” Unity of Interest & Ownership

- Commingling of funds and assets.
- Failure to segregate funds.
- Diversion of funds or assets.
- Treatment by shareholder of corporate assets as own.
- Failure to maintain corporate formalities (*i.e.*, minutes).
- Identical equitable ownership in two entities.
- Officers and Directors of one entity same as controlled corporation.
- Use of the same office or business location.
- Employment of same employees.
- Total absence of corporate assets.
- Gross undercapitalization (at time of formation).
- Use of Corporation as mere shell.
- Instrumentality or conduit for single venture of another corporation.
- Concealment or misrepresentation of the responsible ownership, management and financial interests.
- Concealment or misrepresentation of personal business activities.
- Disregard of legal formalities (*i.e.*, lack of agreements, failure to keep tax filings).
- Failure to maintain arm’s length relationships among related equities.
- The use of the corporate identity to procure labor, services or merchandise for another entity.
- The Diversion of assets from a corporation by or to a stockholder or other person or entity to the detriment of creditors.
- The manipulation of corporate assets and liabilities in entities so as to concentrate the assets in one and the liabilities in another.
- The contracting with another with the intent to avoid performance by use of the corporation entity as a shield against personal liability.
- The use of the corporation as subterfuge for illegal transactions.
- The formation and use of a corporation to transfer to it the existing liability.

Alter Ego

- An “alter ego” is a corporation, organization or other entity set up to provide a **legal shield** for the person or entity actually controlling the operation
- To prevail under the alter ego theory, a plaintiff must prove:
 - One company completely dominated the other with disregard for its separate identity; and
 - An injustice or other wrong to the plaintiff will likely result if the corporate veil is not pierced
 - An example of improper conduct is when a parent establishes a subsidiary as a **mere instrumentality** and a sham to mislead creditors and avoid liability
- Alter ego theory can apply between parent and subsidiary or between sister/affiliated companies

Is the entity being used for purely personal rather than corporate purposes?

Implications for Owners of Healthcare Companies

- CMS and its contractors rarely seek to pierce the corporate veil. However, it has happened in the past.
- In *United States v. Bridle Path Enterprises*, Bridle Path initially made payments towards its Medicare overpayment debt. However, Bridle Path stopped paying its overpayment debt after it sold all of its assets to another provider. At the time of the sale, over \$64,000 was outstanding on the overpayment debt.
- The Massachusetts Federal District Court held the owners **personally liable** for Bridle Path's Medicare overpayment debt by **piercing the corporate veil**. In justifying its decision to pierce the corporate veil, the court emphasized the number of checks Bridle Path wrote to its owners, their home health agency and real estate-holding company. By doing so, the owners failed to treat Bridle Path as a separate corporate entity, warranting veil piercing.

Failure to Maintain Separate Identities

- In *Canter v. Lakewood of Voorhees*, the plaintiff brought a nursing home negligence action against several corporate and individual defendants. The entity that operated the nursing home was a limited partnership (“**Operator**”), and one limited partner, **SHI**, held a majority interest in the Operator. SHI was also the sole shareholder of both **Ozal** (the general partner and minority interest holder in the Operator) and a **management company** that provided consulting services to the nursing home in exchange for a management fee. Certain directors and officers of Ozal were also officers of the operator or the management company from time to time.

Failure to Maintain Separate Identities: *Canter v. Lakewood of Voorhees*

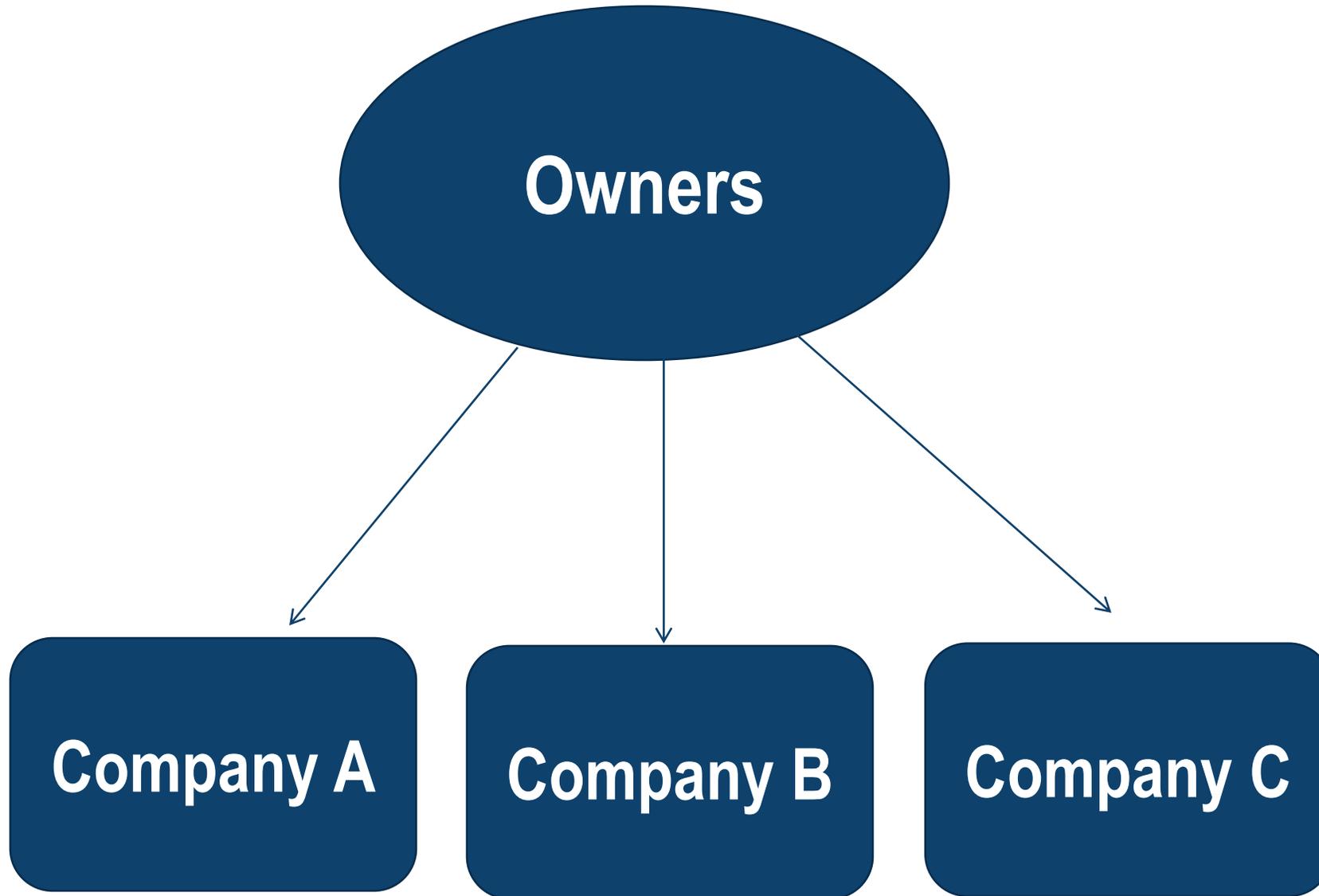
- Plaintiff argued commonality of ownership between parties and shared office involvement established that SHI, through Ozal and the management company, controlled the operations of the nursing home, such that the corporate veil should be pierced.
- The Court disagreed, finding **ownership of a corporation alone is not enough to pierce the corporate veil**
 - No evidence that SHI was substantially involved in the nursing home's day to day operations
 - SHI did not use the operator entity to perpetrate a fraud or injustice

The background of the slide is a grayscale photograph of a medical setting. In the upper portion, a computer monitor displays an ECG (heart rate) graph with several heart icons. Below the monitor, a silver stethoscope is resting on a surface. A dark blue rectangular box is overlaid on the lower half of the image, containing the text 'Case Study 1' in white.

Case Study 1

Case Study 1

- **Company A** is an operator of a CCRC that provides clinical services to the residents of the CCRC and bills payors, including CMS
- **Company B** is a real estate company that owns and leases the property to Company A in exchange for rent, and secured by HUD financing
- **Company C** is engaged in the business of providing comprehensive administrative and management services to healthcare providers, including Company A in exchange for a management fee
- Plaintiff's counsel sues all 3 entities alleging negligent patient care



Legitimate Business Purpose

- Emphasize the legitimate business purpose for the formation and operation of the entities
- Each entity has an independent, different business purpose as set forth in their respective formation documents

Customary Practices

- Emphasize that a particular structure is customary in the applicable state
 - Ex. Separation of clinical operations from real estate or from a company that provides management services to the CCRC is **usual and customary**

Conforming to Industry Regulations

- Relationships between A, B and C were **purposefully structured** to conform to the complexities of the healthcare industry
 - Ex. Medicare requires healthcare providers to annually report payments made to organizations that furnish services, facilities or supplies to the provider, if that organization serving the provider is a related party. Because A, B and C are all owned by the same owners, any payment made by any of the 3 entities under their Management Agreement must be disclosed to CMS on the Medicare cost report.
 - All payments are made under valid contractual arrangements and **do not provide basis that any of the entities are controlled by another other**

Conforming to Industry Regulations (cont.)

- Changes to governing documents and contractual arrangements **necessary to comply with regulatory requirements**
 - Changes to governing documents and contractual arrangements necessary to obtain a HUD-insured mortgage to refinance the property
 - Changes to management agreement required under FHA guidelines to secure the mortgage

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Case Study 2

Case Study 2

- **Company A** is a limited liability company through which licensed physicians provide anesthesiology to hospital in-patients.
 - Enters into independent contractor agreements with individual physicians to provide in-hospital anesthesiology services at facilities with which it has contractual relationships
- **Company A** entered into an Exclusive Management and Administrative Services Agreement with **Company B**. Company B provides comprehensive administrative and management services to physician practice groups like Company A.
- **Company A** contracts with Hospital to provide licensed anesthesiologists to staff Hospital surgery department
- **Company A** leased physician to Hospital sued for medical malpractice by patient of Hospital and patient's counsel sues Company A, B and Hospital

Corporate Practice of Medicine

- Developed by the AMA to ensure only licensed medical professionals practice medicine/prohibit the commercialization of medicine
 - Purpose: protect independent medical judgment
- In states where the CPOM prohibition is enforced, the doctrine impacts how healthcare entities can be structured

“No corporation except where specifically authorized by statute, and within the limits therein prescribed, may secure, provide, or render medical services to individuals...since such would constitute the practice of medicine contrary to law.”

1934-44 Op. Pa. Att’y Gen. 244 (1944), No. 504.

Corporate Practice of Medicine

- In general, the **CPOM prohibits corporations from practicing medicine or employing physicians to provide medical services**
 - Medical professionals may practice medicine only through certain restricted entities and only licensed persons may own shares, partnership interest or membership units in such restricted entities
- Specific state laws vary but generally address:
 - Prohibiting business entities from employing physicians to provide medical care
 - **Requiring entities that provide medical services be owned and operated by licensed medical doctors**
 - Prohibiting professional fee splitting between licensed medical professionals and non-licensed individuals or business entities
 - Management fees stated within management services agreements must be set at fair market value

Industry Standards

- Where a business enterprise involves the provision of medical services, it has become industry standard for the business to establish a **management company** to contract with the professional entity to carry out such services
 - **Business entity** provides management and administrative services in exchange for a management fee from the captive entity
 - **Captive entity** contracts with individual physicians to provide medical services
- Allows for restricted entity to operate without any infringement on the professional judgment of the physicians by an unrestricted business entity and similarly allows healthcare facilities to continue to employ their own operations without influence from the unrestricted entity.

Industry Standards (cont.)

- The “capUnder these “captive models,” a physician must be selected to serve as the shareholder of the PC or member of the professional LLC and appropriate protective provisions are embodied among the management company, the PC/LLC and the physician
- tive entity,” in turn, contracts with individual physicians to provide medical services and also contracts with healthcare facilities to arrange for its contracted physicians to provide medical services at those facilities
- This captive business arrangement has been recognized by the IRS as a business model **designed specifically to comply with state statutes** that limit ownership in professional companies and to comply with applicable state CPOM prohibition laws

Legitimate Business Purpose

- Entities established in Case Study 2 were each **purposefully structured** to adhere to the CPOM prohibition
 - Specifically established for the legitimate business purpose to carry out the delivery of medical services through a qualified organization and the related management/administrative services needed to support that business

Contractual Arrangements Consistent with Similarly Situated Companies

- Demonstrate that the contractual arrangements are consistent with similarly situated companies structured to comply with the applicable regulations
 - Activities of Company A and Company B must be distinct from one another and established to avoid the creation of an arrangement where Company B would **indirectly practice medicine** in contravention of the CPOM prohibition

Independent Medical Judgment

- No contractual arrangement involving either entity causes either entity to direct or control the **independent medical judgment** of or the practice of medicine by any Company A-affiliated physician

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Recent Developments

Andrew Carothers, M.D. v. Progressive Insurance Company

- Dr. Carothers established a PC to provide MRI services. The PC agreed to lease MRI facilities and equipment from companies owned and controlled by non-physicians, which acted as an MSO to the PC.
- The Court examined the arrangement between the PC and MSO and found the terms violated the corporate practice of medicine doctrine making the entity improperly incorporated, thus allowing an insurance company to withhold payment.

An insurer could withhold payments for medical services provided by professional corporations “**when there is willful and material failure to abide by licensing and incorporation statutes**” despite no direct finding of fraud

Andrew Carothers, M.D. v. Progressive Insurance Company (cont.)

■ **Fraudulent Incorporation Factors**

- Equipment leases were far **above FMV**: the difference between the FMV and what was charged in one year was **\$4,680.00**
- MSO had the **right to terminate each lease without cause**, regardless of payment, but the PC could not terminate the leases at all
- Dr. Carothers barely provided **oversight** for the provision of medical services: He did not perform services himself and reviewed at most 79 reports out of 38,000
- Dr. Carothers was not involved with the business operations and, instead, **delegated duties to a non-physician**, who ran the business of the PC, and who funneled millions of dollars to herself and the MSO from the PC's bank account

Andrew Carothers, M.D. v. Progressive Insurance Company (cont.)

- Key Considerations
 - Corporate structure with an MSO must be based on:
 - Fair market value
 - Physicians retaining control over medical decisions
 - Record-keeping best practices
- Liability may be imposed **even without** a direct finding of fraud

Transition Healthcare Assocs. v. Tri-State Health Investors, LLC.

- Proof of some *overlapping management* between subsidiary and parent is an insufficient basis to pierce the corporate veil.
- In Ohio, a mere breach of contract is insufficient to pierce the corporate veil

Welker v. Carnevale

- Parents sued Clearfield Hospital and its affiliates, Penn Highlands Healthcare and Penn Highlands Clearfield, for allegedly causing neurological damage to their child during delivery
- U.S. District Judge Kim Gibson dismissed Penn Highlands Healthcare and Penn Highlands Clearfield from the medical-malpractice suit, saying Pennsylvania laws weigh against piercing the corporate veil of the hospital

Welker v. Carnevale (cont.)

- Emphasized Pennsylvania's strong presumption against piercing the corporate veil
 - No indication that **corporate formalities** were not observed with respect to subsidiaries
 - Nothing in the record to suggest there was a substantial **mingling of corporate and personal affairs or funds**
 - No evidence that corporate form was used to **perpetuate a fraud**

McCoy v. FemPartners, Inc.

- Business arrangement whereby **companies** would manage and administer non-medical operations for a **medical practice**
- Even though the company was entitled to approximately 20% of clinic distribution funds as defined by the service agreement, this constituted payment for the business management and administrative services it provided to the medical practice, **which was completely independent**, and its physicians exercised their own judgment as to patient clinical services
- Court did not pierce the corporate veil

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Recommendations

Closing Comments

- Depending on the type of business created, whether it be corporate, LLC or otherwise, owners must be aware of the formalities that they must adhere to depending on their corporate structure
 - Ensure compliance with corporate formalities
 - Adhere to operating agreement
 - Maintain written documentation of all major business actions, including agreements with 3rd parties
 - Keep business assets and expenditures distinct and separate
 - Observe annual filing requirements

Questions? Thank you!



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