Understanding Bankruptcy as a Tool for the Continued Operation of a Medical Practice

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Medical professionals who own their private practice wear 2 hats: a professional one and a business one. While they are diagnosing and treating patients, they also are running their business, which includes paying salaries and overhead. However, like every business owner, a medical practice may face a myriad of problems that can cause financial difficulties. These problems can range from medically related (eg, malpractice judgments and nonpayment from insurance companies and patients) to nonmedically related (eg, overhead and lawsuits from contractors or former employees). These potential problems can all lead, individually or collectively, to the financial instability of the practice.

Many medical professionals who face financial instability do not consider filing a bankruptcy petition to be a viable option, presumably because of (1) the stigma of bankruptcy, and (2) a lack of understanding of the bankruptcy process. In fact, depending on the circumstances, a bankruptcy filing may be the best way to address these issues and a preferable alternative to shutting down. In all cases, the decision to file for bankruptcy should be discussed with an attorney who specializes in bankruptcy, because many issues can arise in the context of a bankruptcy filing. The purpose of this article is to explain the bankruptcy process and to address issues related to a medical practice's filing with regard to contractual obligations, patient care, and the handling of medical records.

Types of Bankruptcy: Dissolve or Reorganize

There are 2 types of bankruptcy filings that private providers and medical practices can avail themselves of as set forth in title 11 of the United States Code (otherwise referred to as the Bankruptcy Code)—Chapter 7 and Chapter 11. A Chapter 7 bankruptcy is a liquidation bankruptcy wherein the business will cease operating and its assets will be liquidated by a Chapter 7 trustee in order to pay the debtor's creditors. Alternatively, a Chapter 11 bankruptcy is a reorganization bankruptcy. A Chapter 11 debtor is generally referred to as a "debtor-in-possession," because the debtor, such as a medical practice, remains in control of the business and continues to operate it in the ordinary course. During the progression of a Chapter 11 case, the debtor is required to formulate a "plan of reorganization," which sets forth the payments that will be made to the debtor's creditors, the time period that those payments will be made, and how the debtor will make the payments. While some of the things discussed here apply equally in both a Chapter 7 and a Chapter 11 context, for the purposes of this article, we will address the issues set forth below from the perspective of a potential Chapter 11 filing (reorganization) by a medical practice or provider.

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The Automatic Stay

One of the most desirable benefits of filing for bankruptcy protection is the automatic stay (11 USC § 360). The automatic stay goes into effect immediately upon a bankruptcy filing and essentially serves as a "stop work" order for certain civil actions that are being taken against the debtor, such as medical malpractice actions and collection actions. As long as the automatic stay is in effect, barred actions against the bankruptcy filer or debtor will be stalled and new barred actions cannot be commenced. However, the automatic stay is not infinite in duration. A creditor, or an adversary in a lawsuit, can make a motion to the bankruptcy court to vacate the stay. These motions must be done on notice to the debtor and can be opposed. It should be noted that if a medical practice files for bankruptcy, the stay will not act to stay a personal action against the practitioner as the automatic stay applies to the debtor.

In addition, there are exceptions to the automatic stay. The automatic stay does not stop a criminal

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prosecution (or the commencement of one), nor does it stop the suspension or revocation of a professional license, such as a medical license (11 USC § 362[b]: *McMullen v Sevigny*, 386 F3d 320, 325 [1st Cir Mass 2004]).

Another exception arises in the context of a debtor that deals with the Department of Health and Human Services (HHS). Section 362(b)(28) of the Bankruptcy Code provides that the automatic stay does not prevent the Secretary of HHS from excluding a debtor from participating in the Medicare program or in any other federal healthcare program (11 USC § 362[b][28]). By being excluded from the Medicare program, the debtor will be unable to receive payments from Medicare for services rendered to Medicare beneficiaries. Therefore, a debtor attempting to file for bankruptcy protection with the goal of preventing HHS from excluding it from a federal healthcare program would be unsuccessful. Medical professionals and their bankruptcy professionals should be aware of this section, because it may play a role in prepetition bankruptcy planning for the medical practice.

Assumption or Rejection of Unexpired Leases

The largest costs for a medical practice are for the medical equipment and the office space. For example, the costs of a magnetic resonance imaging machine can run into the millions of dollars and result in high monthly lease payments. One provision of the Bankruptcy Code provides that unexpired leases, such as equipment or rental leases, may be either assumed (continued) or rejected by the debtor in bankruptcy (11 USC § 365). A Chapter 11 debtor that wishes to assume or reject a lease will either make a motion to the bankruptcy court seeking approval, or provide for such assumption or rejection in the plan of reorganization. The bankruptcy court will need to determine whether the assumption or rejection is in the best interests of the debtor's creditors. In a scenario where the debtor seeks to reject an equipment lease, the debtor's motion will usually assert that the costs of the equipment lease are too burdensome to sustain and, therefore, it must be rejected to protect the debtor's estate.

> Some of the nonexclusive factors that a court will consider when determining whether to appoint an ombudsman can range from the cause of the debtor's bankruptcy filing, the debtor's history of patient care, and the potential for patient injury if the debtor were to drastically reduce its level of care.

Subsequent to any rejection, the lessor will have an unsecured claim against the debtor's estate for the sum that was not paid before the bankruptcy filing, as well as an administrative claim for the sum that was not paid during the bankruptcy case. These debts will be paid off in accordance with the reorganization plan, and the debtor will no longer have to make the lease payments that were due after the rejection date. The ability of a debtor to assume or reject a lease is a powerful one in a Chapter 11 context, and can be used to alleviate some of the financial burdens that may have pushed the medical practice into bankruptcy.

Potential Appointment of an Ombudsman

Although many aspects of a Chapter 11 bankruptcy filing are standard, regardless of the debtor and its business, there are distinct differences that must be addressed if the debtor is classified as a "healthcare business." Under the Bankruptcy Code, a *healthcare business* is defined as either a public or a private entity that is "primarily engaged in…the diagnosis or treatment of injury, deformity, or disease; and surgical, drug treatment, psychiatric, or obstetric care" (11 USC § 101[27A]). This is further defined to include any general or specialized hospital; any ancillary ambulatory, emergency, or surgical treatment facility; hospices; home health agencies or similar entities; and any long-term care facility, such as nursing homes (11 USC § 101[27A]). Examples of a healthcare business can range from a medical practice that operates multiple locations to a solo practice that provides plastic surgery to its patients (*In re N Shore Hematology-Oncology Assocs, PC*, 400 BR 7 [Bankr EDNY 2008]; *In re William L. Saber, MD, PC*, 369 BR 631 [Bankr D Colo 2007]; *In re Med Assocs of Pinellas*, LLC, 360 BR 356 [Bankr MD Fla 2007]). Therefore, potential bankruptcy filers should discuss all aspects of

their practice with their counsel to ensure that it is classified correctly and that the appropriate procedures are being followed pursuant to the Bankruptcy Code.

One aspect of a Chapter 11 bankruptcy filing of a healthcare business is the potential for a court appointment of a patient care ombudsman (11 USC § 333). This is an individual tasked with monitoring the quality of patient care that is provided by the debtor, and representing the patients' interests during the course of the bankruptcy case (11 USC § 333[a][1]. A court determination of whether to appoint a patient care ombudsman is a fact-intensive, case-specific inquiry. Some of the nonexclusive factors that a court will consider when determining whether to appoint an ombudsman can range from the cause of the debtor's bankruptcy filing, the debtor's history of patient care, and the potential for patient injury if the debtor were to drastically reduce its level of care (*In re Alternate Family Care*, 377 BR 754, 758 [Bankr SD Fla 2007]; *In re N Shore Hematology-Oncology Assocs, PC*, 400 BR 7,8 [Bankr EDNY 2008]).

If appointed, the patient care ombudsman generally conducts interviews with both the patients and the physicians in the medical practice or organization (11 USC § 333[b][1]). Any information that is obtained relating to the patients, including their medical records, is confidential (11 USC § 333[c][1]). Although the patient care ombudsman does not have immediate authority to review these patient records, the bankruptcy court may authorize him or her to do so subject to certain restrictions to be determined by the court (11 USC § 333[c][1]). During the course of his or her review, the patient care ombudsman reports to the bankruptcy court every 60 days regarding the quality of the care that is being provided to patients, and may intervene, if necessary, if a crisis arises with a patient or if there are disputes regarding a patient's care (11 USC § 333[b][2]).

Treatment of Patient Records

Another source of concern for the medical practice and for its patients is what will happen to the patient records if there is a bankruptcy filing. Although patient records legally belong to the patient, the medical practice holds the records in physical and, usually, in digital form. The Bankruptcy Code specifically addresses the treatment of patient records if the debtor is deemed a healthcare business and cannot financially maintain them in accordance with federal law (11 USC § 351). Under the Bankruptcy Code, the debtor must publish a notice in at least 1 newspaper that informs the public that the debtor has filed for bankruptcy and that the debtor's patients have 1 year to claim their medical records before the records are destroyed (11 USC § 351[3]). During the first 180 days of that 365-day period, the debtor must mail a notice to each patient's last known address, as well as to each patient's insurance carrier, alerting them of the potential destruction of their medical records (11 USC § 351[3]). Before the records are destroyed, the debtor must make 1 last attempt to preserve them by submitting a request to an appropriate government agency to store the unclaimed records. If the request is not granted, the records can then be destroyed.

However, if the debtor is not considered to be a healthcare business, the debtor will still need to address the issue of patient records in accordance with the Health Insurance Portability and Accountability Act (HIPAA) of 1996 Privacy and Security Rules, as well as other relevant federal and state laws. For example, New York requires the retention of patient records for 6 years (NY Comp Codes R & Regs Tit 8, § 29.2[a][3]). As such, it is important for medical practitioners to work with their bankruptcy attorneys and healthcare attorneys to ensure compliance with these laws.

Conclusion

Bankruptcy, often a misunderstood and dismissed option for medical professionals in a financial crunch, may, in fact, be used as a beneficial tool for the continued operation or orderly closure of a medical practice. Deciding whether bankruptcy is an option for your practice requires working with an experienced bankruptcy attorney to review relevant factors to your operations that can run the gamut of medical equipment leases to patient records. ●

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