Department of Health and Human Services

DEPARTMENTAL APPEALS BOARD

Civil Remedies Division

In the Cases of: The Inspector General, - v. - Hanlester Network, et al. (Nos. C-186 through C-192); and Melvin L. Huntsinger, M.D. (No. C-208) and Ned Welsh (No. C-213), Respondents.	DATE: March 1, 1991 Docket Nos. C-186 through C-192, No. C-208 and C-213 Decision No. CR118

DECISION

Respondents requested hearings to contest the Inspector General's (the I.G.) proposal to exclude them from participating in Medicare and any State health care program.[1] The I.G. alleged that Respondents violated sections 1128B(b)(1) and (b)(2) of the Social Security Act (the Act), and that exclusions were therefore authorized by section 1128(b)(7) of the Act. The I.G. requested that I impose and direct exclusions against Respondents for periods ranging from three years to permanent.

I decided to consolidate these cases because there were issues of fact and law which were common to all of them. I held a consolidated hearing in Van Nuys, California from August 14 to 27, 1990. Based on the

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[1] "State health care program" is defined by section 1128(h) of the Social Security Act to cover three types of federally-assisted programs, including State plans approved under Title XIX (Medicaid) of the Act. I use the term "Medicaid" hereafter to represent all State health care programs encompassed by the I.G.'s proposed exclusion of Respondents.

law, regulations, and evidence adduced at the hearing of these cases, I conclude that the I.G. proved that Respondents The Hanlester Network, Pacific Physicians Clinical Laboratory, Ltd., Omni Physicians Clinical Laboratory, Ltd., and Placer Physicians Clinical Laboratory, Ltd. knowingly and willfully offered remuneration to physicians to induce them to refer program-related business in violation of section 1128B(b)(2) of the Act. I conclude that the I.G. did not prove that Respondents Kevin Lewand, Gene Tasha, Ned Welsh, Melvin L. Huntsinger, M.D., or Keorle Corp. knowingly and willfully offered or paid remuneration to physicians to induce them to refer program-related business in violation of section 1128B(b)(2) of the Act. I conclude that the I.G. did not prove that any of Respondents knowingly and willfully solicited or received remuneration in return for referring program-related business in violation of section 1128B(b)(1) of the Act. I conclude that no remedial purpose would be served by imposing or directing exclusions in this case. Therefore, I neither impose nor direct an exclusion against any Respondent.

As a convenience, a table of contents is set forth below.

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ISSUES

The issues in these cases are whether:

1. any Respondent knowingly and willfully solicited or received remuneration in return for referring program-related business in violation of section 1128B(b)(1) of the Act;

2. any Respondent knowingly and willfully offered or paid remuneration in order to induce physicians to refer program-related business in violation of section 1128B(b)(2) of the Act;

3. a remedial purpose would be served by imposing or directing an exclusion against any Respondent from participating in the Medicare and Medicaid programs.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

1. The Respondents in these cases are: The Hanlester Network (Respondent Hanlester); Keorle Corp. (Respondent Keorle); Pacific Physicians Clinical Laboratory, Ltd. (Respondent PPCL); Omni Physicians Clinical Laboratory, Ltd. (Respondent Omni); Placer Physicians Clinical Laboratory, Ltd. (Respondent Placer); Kevin Lewand (Respondent Lewand); Gene Tasha (Respondent Tasha); Melvin L. Huntsinger, M.D. (Respondent Huntsinger); and Ned Welsh (Respondent Welsh).

2. Respondent Keorle is a California corporation whose shareholders include Respondent Lewand. Tr. at 1940.[2]

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[2] The parties' exhibits and the transcript of the proceedings in these cases will be cited as follows:

Inspector General Exhibit	I.G. Ex. (number)/(page)
Respondents Hanlester, Keorle, PPCL, Omni, Placer, Lewand, Tasha Exhibit	Ha. Ex. (number)/(page)
Respondent Welsh Exhibit	We. Ex. (number)/(page)
Respondent Huntsinger Exhibit	Hu. Ex. (number)/(page)
Transcript	Tr. at (page)

3. Prior to January, 1989, Respondent Keorle was known as the Hanlester Corporation. Tr. at 1975-76.

4. Respondent Hanlester is a general partnership organized under California law. I.G. Ex. 4.0/22.

5. Respondent Hanlester was formed on January 1, 1987. Tr. at 1975.

6. The original general partners in Respondent Hanlester were the Hanlester Corporation, James A Padova, M.D., Inc., a California medical corporation, Respondent Tasha, and Respondent Welsh. I.G. Ex. 4.0/22.

7. Hanlester Corporation owned a majority interest in Respondent Hanlester. See I.G. Ex. 115.0; Tr. at 2169; see Tr. at 1941.

8. Hanlester Corporation sold its interest in Respondent Hanlester to Respondent Tasha in January, 1989. See Tr. at 1976.

9. Until January, 1989, Respondent Lewand served as President of Respondent Hanlester. I.G. Ex. 2.0/7; see Tr. at 1940 - 1948, 1976.

10. Respondent Tasha served as Vice-President, Operations, of Respondent Hanlester. I.G. Ex. 2.0/7.

11. Respondent Welsh served as Vice-President, Business Development, of Respondent Hanlester. I.G. Ex. 2.0/7.

12. Respondent Welsh ceased being a general partner or executive in Respondent Hanlester in the summer of 1987. See I.G. Ex. 17.1/17; see Tr. at 2002.

13. Respondent Hanlester represented that Respondent Huntsinger served as its medical director. I.G. Ex. 3.0.

14. On March 26, 1987, Respondent Hanlester issued a private placement memorandum for Respondent PPCL. I.G. Ex. 4.0.

15. The purpose of the private placement memorandum was to offer limited partnership shares in Respondent PPCL. I.G. Ex. 4.0/1, 7.

16. Respondent PPCL was a limited partnership organized under the laws of California. I.G. Ex. 4.0/7.

17. A purpose for which Respondent PPCL was organized was to own a clinical laboratory located in the Los Angeles - Orange County, California, area. I.G. Ex. 4.0/7.

18. The general partner in Respondent PPCL was Respondent Hanlester. I.G. Ex. 4.0/22.

19. Respondent Hanlester had exclusive authority to make all management decisions with respect to Respondent PPCL. I.G. Ex. 4.0/29.

20. Respondent Huntsinger was an initial limited partner in Respondent PPCL, and owned 30 limited partnership shares. I.G. Ex. 4/40; Tr. at 2290.

21. On January 31, 1988, Respondent Hanlester issued a private placement memorandum for Respondent Omni. I.G. Ex. 5.0.

22. The purpose of the private placement memorandum was to offer limited partnership shares in Respondent Omni. I.G. Ex. 5.0/1, 7.

23. Respondent Omni was a limited partnership organized under the laws of California. I.G. Ex. 5.0/7.

24. A purpose for which Respondent Omni was organized was to own a clinical laboratory in or near Pasadena, California. I.G. Ex. 5.0/8.

25. The general partner in Respondent Omni was Respondent Hanlester. I.G. Ex. 5.0/23.

26. Respondent Hanlester had exclusive authority to make all management decisions for Respondent Omni. I.G. Ex. 5.0/31.

27. On March 1, 1988, Respondent Hanlester issued a private placement memorandum for Respondent Placer. I.G. Ex. 6.0.

28. The purpose of the private placement memorandum was to offer limited partnership shares in Respondent Placer. I.G. Ex. 6.0/1, 7.

29. Respondent Placer was a limited partnership organized under the laws of California. I.G. Ex. 6.0/7.

30. A purpose for which Respondent Placer was organized was to own a clinical laboratory in either Roseville or Sacramento, California. I.G. Ex. 6.0/8.

31. The general partner in Respondent Placer was Respondent Hanlester. I.G. Ex. 6.0/23.

32. Respondent Hanlester had exclusive authority to make all management decisions for Respondent Placer. I.G. Ex. 6.0/32.

33. Respondent Hanlester offered investors limited partnership shares in Respondents PPCL, Omni, and Placer. I.G. Ex. 4.0/1, 7, 9, 10; I.G. Ex. 5.0/1, 7, 9, 10; I.G. Ex. 6.0/1, 7, 9, 10.

34. Respondent Hanlester offered a total of 600 limited partnership shares in Respondent PPCL, with the offering price being $500 per share. I.G. Ex. 4.0/1.

35. Respondent Hanlester offered a total of 800 limited partnership shares in Respondent Omni, with the offering price being $500 per share. I.G. Ex. 5.0/1.

36. Respondent Hanlester offered a total of 800 limited partnership shares in Respondent Placer, with the offering price being $500 per share. I.G. Ex. 6.0/1.

37. The minimum investment offered by Respondent Hanlester to a potential purchaser of limited partnership shares in either Respondent PPCL, Respondent Omni, or Respondent Placer, was three shares. I.G. Ex. 4.0/1; I.G. Ex. 5.0/1; I.G. Ex. 6.0/1.

38. Respondent Hanlester limited the number of purchasers in each limited partnership (Respondents PPCL, Omni, and Placer) to a maximum of 35 individuals or entities. I.G. Ex. 4.0/7; I.G. Ex. 5.0/7; I.G. Ex. 6.0/7.

39. Respondent Hanlester restricted its limited partnership offering in Respondent PPCL to licensed physicians residing in California who actively practiced medicine in Los Angeles or Orange County, and to California medical corporations and partnerships consisting of physicians or entities whose ownership of

shares would, in Respondent Hanlester's judgment, benefit Respondent PPCL. I.G. Ex. 4.0/7.

40. Respondent Hanlester restricted its limited partnership offering in Respondent Omni to licensed physicians residing in California who actively practiced medicine in the north and eastern portions of Los Angeles County and to California medical corporations and partnerships consisting of physicians or entities whose ownership of shares would, in Respondent Hanlester's judgment, benefit Respondent Omni. I.G. Ex. 5.0/7.

41. Respondent Hanlester restricted its limited partnership offering in Respondent Placer to licensed physicians residing in California who actively practiced medicine in the Sacramento metropolitan area and to California medical corporations and partnerships consisting of physicians or entities whose ownership of shares would, in Respondent Hanlester's judgment, benefit Respondent Placer. I.G. Ex. 6.0/7.

42. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that, initially, substantially all business would be obtained from the limited partners and that partnership business would be obtained primarily from the limited partners. I.G. Ex. 4.0/8, 16, 18; I.G. Ex. 5.0/8 - 9, 16 - 17, 19; I.G. Ex. 6.0/8 - 9, 17, 19.

43. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that physicians who regularly ordered outpatient tests would be sought as limited partners. I.G. Ex. 4.0/8; I.G. Ex. 5.0/8 - 9; I.G. Ex. 6.0/8 - 9.

44. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that if they purchased partnership shares but did not utilize the partnerships' laboratories, it would be a "blueprint for failure" of the laboratories. I.G. Ex. 2.0/6; I.G. Ex. 3.0.

45. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that business would also be solicited from non-partner physicians. I.G. Ex. 4.0/8; I.G. Ex. 5.0/8 - 9; I.G. Ex. 6.0/8 - 9.

46. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that patronage of the partnerships' laboratories by limited

partners was voluntary. I.G. Ex. 4.0/18; I.G. Ex. 5.0/19; I.G. Ex. 6.0/19.

47. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that, under California law, it would be illegal to offer or pay consideration to a physician to induce or compensate that physician to refer patients to a laboratory. I.G. Ex. 4.0/4; I.G. Ex. 5.0/4; I.G. Ex. 6.0/4.

48. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that returns on investment in the limited partnerships would not be based on partners' patient referrals, but would be based on the profits earned by the partnerships. I.G. Ex. 4.0/4; I.G. Ex. 5.0/5; I.G. Ex. 6.0/5.

49. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that the partnerships' success in obtaining referrals from limited partners would depend on the partnerships' laboratories performing outpatient testing and laboratory analysis in a timely and dependable manner at competitive rates. I.G. Ex. 4.0/28; I.G. Ex. 5.0/30; I.G. Ex. 6.0/31.

50. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that failure by the partnerships' laboratories to perform outpatient testing and laboratory analysis in a timely and dependable manner at competitive rates could result in the limited partners, who had a primary duty to their patients, referring their laboratory testing to laboratories other than the partnerships' laboratories. I.G. Ex. 4.0/28 - 29; I.G. Ex. 5.0/30; I.G. Ex. 6.0/31.

51. Respondent Hanlester told prospective limited partners in Respondent PPCL that their annual income per share could range from $266 to $532, depending on factors including the number of shares sold, annual receipts, and operating costs. I.G. Ex. 4.0/37.

52. Respondent Hanlester told prospective limited partners in Respondents Omni and Placer that their annual income per share could range from about $200 to about $400, depending on factors including the number of shares sold, annual receipts, and operating costs. I.G. Ex. 5.0/39 - 40; I.G. Ex. 6.0/40 - 41.

53. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni and Placer that, based on estimates contained in the private placement memorandums, they could expect an annual profit of greater than 50% of their investment. I.G. Ex. 2.0/5; see I.G. Ex. 4.0/37; I.G. Ex. 5.0/39 - 40; I.G. Ex. 6.0/40 -41.

54. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that there could be no assurance that the partnerships would operate on a profitable basis or attain projected income levels. I.G. Ex. 4.0/19; I.G. Ex. 5.0/20; I.G. Ex. 6.0/20.

55. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that projected profits were not based on historical data, but were based on assumptions regarding business volume and estimated costs. I.G. Ex. 4.0/27; I.G. Ex. 5.0/29; I.G. Ex. 6.0/30.

56. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that purchase of shares involved a high degree of risk. I.G. Ex. 4.0/2; I.G. Ex. 5.0/2; I.G. Ex. 6.0/2.

57. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that they should consider purchasing shares only if they could afford a total loss of their investment. I.G. Ex. 4.0/2; I.G. Ex. 5.0/2; I.G. Ex. 6.0/2.

58. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that there were investment risks associated with the manner in which the partnerships' income and expenses were considered for tax purposes by the Internal Revenue Service. I.G. Ex. 4.0/26 - 27; I.G. Ex. 5.0/27 - 29; I.G. Ex. 6.0/28 - 30.

59. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that there were investment risks associated with the operation of the partnerships' laboratories, including the absence of operating histories and competition from other laboratories. I.G. Ex. 4.0/27 - 29; I.G. Ex. 5.0/29 - 31; I.G. Ex. 6.0/30 - 32.

60. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that there were investment risks associated with reliance on

the management decisions of Respondent Hanlester. I.G. Ex. 4.0/29 - 30; I.G. Ex. 5.0/31; I.G. Ex. 6.0/32.

61. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that it had negotiated a subcontract with SmithKline Bio-Science Laboratories, Inc. (SKBL) which gave SKBL the option to manage the partnerships' laboratories. I.G. Ex. 4.0/16 - 17; I.G. Ex. 5.0/17 - 18; I.G. Ex. 6.0/17 - 18.

62. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that management of the partnerships' laboratories by SKBL would assure that all medical tests would be performed according to the highest standards attainable. I.G. Ex. 4.0/17; I.G. Ex. 5.0/18; I.G. Ex. 6.0/18.

63. Respondent Hanlester told prospective limited partners in Respondents PPCL, Omni, and Placer that the private placement memoranda issued for the limited partnerships were the only sales material which could be used in connection with the sale of shares. I.G. Ex. 4.0/10; I.G. Ex. 5.0/10; I.G. Ex. 6.0/10.

64. Richard Aprahamian served as attorney for Respondents Lewand and Hanlester. Tr. at 2176 - 2177.

65. Mr. Aprahamian prepared the private placement memoranda which Respondent Hanlester issued for Respondents PPCL, Omni, and Placer. Tr. at 2177 - 2188; see I.G. Ex. 4.0, I.G. Ex. 5.0; I.G. Ex. 6.0.

66. Mr. Aprahamian met with Respondents Tasha and Welsh to discuss the terms of the private placement memoranda and to advise them as to what they could say to prospective limited partners in Respondents PPCL, Omni, and Placer. Tr. at 2178 - 2179; see I.G. Ex. 4.0; I.G. Ex. 5.0; I.G. Ex. 6.0.

67. Mr. Aprahamian also met with Patricia Hitchcock to discuss the terms of the private placement memoranda and to advise her as to what she could say to prospective limited partners in Respondents PPCL, Omni, and Placer. Tr. at 2178; see I.G. Ex. 4.0; I.G. Ex. 5.0; I.G. Ex. 6.0.

68. Ms. Hitchcock was Respondent Hanlester's Vice President of Marketing and owned four limited partnership shares of Respondent PPCL. I.G. Ex. 3.0/1; Tr. at 941, 943 - 944.

69. Ms. Hitchcock's duties included selling partnership shares in Respondents PPCL, Omni, and Placer. Tr. at 942, 946.

70. Ms. Hitchcock was compensated by Respondent Hanlester for her sales efforts. Tr. at 942.

71. Respondent Hanlester's compensation to Ms. Hitchcock consisted of $3,000.00 a month, expenses for use of an automobile, seven percent of the price of partnership shares she sold, and one percent of the dollar volume of tests referred by physicians to joint venture laboratories. Tr. at 942 - 943.

72. Ms. Hitchcock's compensation from Respondent Hanlester in part depended on the dollar amount of business referred to joint venture laboratories by physicians. Tr. at 943; Finding 71.

73. Mr. Aprahamian met with Respondent Tasha, Respondent Welsh, and Ms. Hitchcock individually and as a group. Tr. at 2179.

74. Meetings between Mr. Aprahamian, Respondent Tasha, Respondent Welsh, and Ms. Hitchcock first occurred early in 1987 in connection with the marketing of limited partnership shares in Respondent PPCL. Tr. at 2179, 2180; see I.G. Ex. 4.0.

75. Mr. Aprahamian also spoke with Ms. Hitchcock on several occasions to respond to her questions concerning what advice and information she could give to prospective limited partners in Respondents PPCL, Omni, and Placer. Tr. at 2179 - 2184.

76. Mr. Aprahamian told Respondent Tasha, Respondent Welsh, and Ms. Hitchcock that they should not make any representations to potential limited partners beyond what was contained in the private placement memoranda. Tr. at 2180 - 2181.

77. Respondent Lewand told Ms. Hitchcock that the only information she could provide potential limited partners in Respondents PPCL, Omni, and Placer was that which was contained in the private placement memoranda. Tr. at 954, 2024E.

78. Respondents Tasha and Welsh told Ms. Hitchcock that, in connection with sales presentations she made to potential limited partners, she should provide potential limited partners with information contained in the private placement memoranda. Tr. at 982 - 983.

79. Mr. Aprahamian told Respondent Tasha, Respondent Welsh, and Ms. Hitchcock, in the presence of Respondent Lewand, that the number of shares offered to a prospective limited partner could not be based on the volume of business that the prospective limited partner was going to refer to a joint venture laboratory. Tr. at 2183 - 2185.

80. Respondents Hanlester, Lewand, Tasha, and Welsh intended that limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer would be physicians who would refer business to a joint venture laboratory. Tr. at 956; Findings 42, 43.

81. Respondents Hanlester, Lewand, Tasha, and Welsh encouraged prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer to refer business to a joint venture laboratory by advising prospective partners that the laboratory's success would depend on such referrals. Findings 42 -44.

82. Respondents Hanlester, Lewand, Tasha, and Welsh did not intend to condition ownership of limited partnership shares in Respondent PPCL, Respondent Omni, or Respondent Placer on the agreement of prospective partners to refer business to a joint venture laboratory. See Findings 46, 47, 66, 67, 73 - 79.

83. Respondents Hanlester, Lewand, Tasha, and Welsh did not intend to condition the number of shares that a prospective partner could own in Respondent PPCL, Respondent Omni, or Respondent Placer on the volume of business that the prospective partner agreed to refer to a joint venture laboratory. See Findings 46, 47, 66, 67, 73 - 79.

84. Respondents Hanlester, Lewand, Tasha, and Welsh did not intend to represent to prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer that there would be little risk associated with their investment in a joint venture. See Findings 56 - 60, 66, 67, 73 - 79.

85. The I.G. did not prove that Respondent Huntsinger was involved in management decisions for Respondent Hanlester as to what offers or representations would be made to prospective limited partners in Respondents PPCL, Omni, and Placer. See Findings 6 - 7.

86. Respondent Welsh made sales presentations on Respondent Hanlester's behalf for the sale of shares in Respondent PPCL. Tr. at 950.

87. The I.G. did not prove that Respondent Welsh told prospective limited partners in Respondent PPCL that the sale of shares would be conditioned on the prospective partner's agreement to refer business to a joint venture laboratory. See Tr. at 1485 - 1486; see Findings 66, 73, 76, 79.

88. The I.G. did not prove that Respondent Welsh told prospective limited partners in Respondent PPCL that the number of shares which they could buy would be based on the volume of business that they would refer to a joint venture laboratory. See Tr. at 1485 - 1486; see Findings 66, 73, 76, 79.

89. The I.G. did not prove that Respondent Welsh told prospective limited partners in Respondent PPCL that there would be little risk associated with their ownership of shares or that returns on their shares would be virtually guaranteed. See Tr. at 1485 - 1486; see Findings 66, 73, 76, 79.

90. Ms. Hitchcock served as Respondent Hanlester's Vice President of Marketing until November, 1988. I.G. Ex. 3.0; Tr. at 942.

91. Ms. Hitchcock made sales presentations on behalf of Respondents Hanlester, PPCL, Omni, and Placer for the sale of shares in Respondents PPCL, Omni, and Placer. Tr. at 941, 942, 946.

92. In her sales presentations, Ms. Hitchcock represented herself to be Respondent Hanlester's Vice President of Marketing and offered to sell limited partnership shares on behalf of Respondents Hanlester, PPCl, Omni, and Placer. I.G. Ex. 3.0, I.G. Ex. 110.0/2 - 3; Tr. at 952.

93. Ms. Hitchcock was authorized by Respondent Hanlester to sell between three and ten shares in Respondent PPCL, Respondent Omni, or Respondent Placer to a prospective limited partner, subject to Respondent Lewand's final approval. Tr. at 989.

94. In her sales presentations to prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer, Ms. Hitchcock told some of them that they could anticipate an annual return of 300 - 400 percent on the purchase price of shares. Tr. at 985 - 986.

95. In her sales presentations to prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer, Ms. Hitchcock told some of them that the return on their investment would be virtually guaranteed. Tr. at 986.

96. In her sales presentations to prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer, Ms. Hitchcock told some of them that an "off the record" condition of sale was that the number of shares sold to a prospective limited partner would be based on the anticipated volume of business that that partner would refer to a joint venture laboratory. Tr. at 995 - 996.

97. The I.G. did not prove that, in her sales presentations to prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer, Ms. Hitchcock told some of them that a prospective limited partner must agree to refer business to a joint venture laboratory as a condition for purchasing limited partner shares. See I.G. Ex. 78.0, 81.0, 109.0/9 - 11, 110.0/6; Tr. at 773, 1451, 1472, 1522, 1614.

98. In her sales presentations to prospective partners in Respondent PPCL, Respondent Omni, or Respondent Placer, Ms. Hitchcock told some of them that limited partners who did not refer business to a joint venture laboratory would be pressured by Respondent Hanlester to either increase their referrals or sell back their shares to Respondent Hanlester. See I.G. Ex. 109.0/9 - 11, 110/6; Tr. at 1122, 1129.

99. Ms. Hitchcock was not authorized by Respondents Hanlester, Lewand, Welsh, or Tasha to tell prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer that they could anticipate an annual return of 300 - 400 percent on the purchase price of shares. Tr. at 1130; Findings 73 - 79.

100. Ms. Hitchcock was not authorized by Respondents Hanlester, Lewand, Welsh, or Tasha to tell prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer that the return on their investment would be virtually guaranteed. Findings 73 - 79.

101. Ms. Hitchcock was not authorized by Respondents Hanlester, Lewand, Welsh, or Tasha to tell prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer that the number of shares that a

prospective limited partner could purchase would depend on the amount of business that the partner would refer to a joint venture laboratory. Findings 73 - 79.

102. Ms. Hitchcock was not authorized by Respondents Hanlester, Lewand, Welsh, or Tasha to tell prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer that if they did not refer business to a joint venture laboratory they would be pressured by Respondent Hanlester to sell back their shares. Findings 73 - 79.

103. The I.G. did not prove that Respondents Hanlester, Lewand, Welsh, or Tasha knew that Ms. Hitchcock told prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer that they could anticipate an annual return of 300 - 400 percent on the purchase price of shares. See Tr. at 1130, 2024I - 2024O

104. The I.G. did not prove that Respondents Hanlester, Lewand, Welsh, or Tasha knew that Ms. Hitchcock told prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer that the return on their investment would be virtually guaranteed. See Tr. at 2024I - 2024O

105. The I.G. did not prove that Respondents Hanlester, Lewand, Welsh, or Tasha knew that Ms. Hitchcock told prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer that the number of shares that a prospective limited partner could purchase would depend on the amount of business that that partner would refer to a joint venture laboratory. See Tr. at 994 - 1002, 2024I - 2024O.

106. The I.G. did not prove that Respondents Hanlester, Lewand, Welsh, or Tasha knew that Ms. Hitchcock told prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer that if they did not refer business to a joint venture laboratory they would be pressured by Respondent Hanlester to sell back their shares. See Tr. at 2024I - 2024O.

107. Ms. Hitchcock ceased working for Respondent Hanlester in November 1988. Tr. at 942.

108. Respondent Tasha made sales presentations on Respondent Hanlester's behalf for the sale of shares in Respondents PPCL, Omni, and Placer. Tr. at 2215.

109. Respondent Tasha did not tell prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer that they must agree to refer business to a joint venture laboratory as a condition of purchasing shares. Tr. at 2215.

110. Respondent Tasha did not tell prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer that the number of shares that they would be permitted to purchase would depend on the amount of business they agreed to refer to a joint venture laboratory. Tr. at 2215 - 2216.

111. On behalf of Respondent Hanlester, Respondent Huntsinger contacted physicians to determine whether they were interested in purchasing shares in Respondent PPCL, Respondent Omni, or Respondent Placer. Tr. at 2296.

112. Respondent Huntsinger did not make sales presentations to prospective limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer on behalf of Respondent Hanlester. Tr. at 2297 - 2299.

113. Respondent Huntsinger was not employed by Respondent Lewand, Respondent Welsh, Respondent Tasha, Respondent Hanlester, Respondent PPCL, Respondent Omni, or Respondent Placer. See Tr. at 2294.

114. Respondent Huntsinger had a contract with SKBL to serve as medical director of Respondent PPCL and Respondent Omni. Tr. at 2294.

115. It was in the pecuniary interest of Respondent Hanlester and its general partners that limited partners in Respondents PPCL, Omni, and Placer refer business to joint venture laboratories. I.G. Ex. 3.0, 4.0, 5.0, 6.0.

116. Respondent Lewand loaned three physicians the amount of the purchase price of the shares that they purchased in Respondent PPCL. I.G. Ex. 10.0, 11.0; Tr. at 2024Q - 2024S.

117. The payment provisions of these loans were subsequently modified to permit the borrowers to pay off the loans by crediting their limited partnership distributions against the principal amounts. Tr. at 2104 -2105; see I.G. Ex. 10.1, 11.1.

118. Respondent Lewand made these loans because Ms. Hitchcock had told the borrowers that they would be loaned the funds to purchase shares in Respondent PPCL. Tr. at 2024Q - 2024S.

119. Respondent Hanlester monitored limited partners' usage of joint venture laboratories. I.G. Ex. 109.0/11; Tr. at 546, 911 - 914, 2024N.

120. In the Spring and Summer of 1988, Respondents Tasha and Lewand attempted to resolve problems that physicians experienced with the quality of services provided by joint venture laboratories. Ha. Ex. 40, 41; Tr. at 2216.

121. Respondents PPCL, Omni, and Placer experienced problems with the quality of service that was being provided to physicians who referred laboratory tests. Tr. at 2216; Finding 120.

122. Problems included failure to pick up laboratory tests. Tr. at 2216 - 2217.

123. Problems also included problems with billing and collecting for laboratory services. Tr. at 2010 - 2011, 2232; Finding 120.

124. Respondent Tasha requested Respondent Huntsinger to telephone physicians whose referrals to joint venture laboratories had decreased. Tr. at 2231 - 2232.

125. Respondent Huntsinger made telephone calls to limited partners in Respondent PPCL and Respondent Omni in his capacity as medical director. Tr. at 2302.

126. The purpose of these calls was to resolve problems that limited partners were experiencing concerning their use of joint venture laboratories. Tr. at 2302.

127. Respondent Huntsinger asked limited partners to explain why they did not refer more business to joint venture laboratories. Tr. at 768, 1562 - 1563, 1830.

128. Respondent Huntsinger told limited partners that they were not referring sufficient business to joint venture laboratories, based on comparing their referrals to referrals made by other limited partners. Tr. at 1455, 1489.

129. Respondent Huntsinger told limited partners that their failure to make sufficient referrals to a joint venture laboratory was hurting the interests of other limited partners. Tr. at 1489.

130. The I.G. did not prove that Respondent Huntsinger told limited partners in Respondent PPCL or Respondent Omni that they must refer business to a joint venture laboratory as a condition for owning shares. See Findings 124 - 127.

131. The I.G. did not prove that Respondent Huntsinger told limited partners in Respondent PPCL or Respondent Omni that they must increase their referrals to a joint venture laboratory as a condition for owning shares. See Findings 124 - 127.

132. The I.G. did not prove that Respondent Huntsinger threatened limited partners in Respondent PPCL or Respondent Omni that the purchase price of their shares would be returned to them and their limited partnerships would be terminated unless they utilized joint venture laboratories. See Findings 124 - 127.

133. At a meeting of limited partners in December 1987, a limited partner asked Respondent Lewand the consequences which could result from a limited partner not referring business to a joint venture laboratory. Tr. at 2019.

134. Respondent Lewand answered the question by stating that the fact that a physician does not refer tests to a joint venture laboratory is not grounds for his removal as a limited partner. Tr. at 2020.

135. Respondent Lewand further stated that the basis for repurchase of a limited partner's shares in Respondent PPCL, Respondent Omni, or Respondent Placer would be that partner's death, retirement, closing his practice, or if 51 percent of the partners agreed that it would be detrimental to the partnership's interest for the limited partner to remain. Tr. at 2020; see Tr. at 1644, 1648.

136. The I.G. did not prove that Respondent Lewand told limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer that their shares would be repurchased if they failed to refer business to a joint venture laboratory. See Findings 133 - 135.

137. The I.G. did not prove that Respondent Hanlester, Respondent Tasha, or Respondent Welsh told limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer that their shares would be repurchased if they failed to refer business to a joint venture laboratory. See We Ex. 37, 38,39, 40; I.G. Ex. 39.0; Tr. at 429 - 432, 502 - 503, 505, 510, 806, 836 - 837, 2126, 2217; Findings 109, 110, 125 - 130, 133 - 135.

138. Respondent Hanlester returned the purchase price of shares to some limited partners in Respondent PPCL after they had telephone conversations with Respondent Huntsinger concerning the amount of business they referred to a joint venture laboratory. I.G. Ex. 13.0; Tr. at 769, 1457, 1563 - 1564, 1831.

139. Some limited partners in Respondent PPCL did not refer business to a joint venture laboratory, but remained limited partners in Respondent PPCL. Tr. at 825 - 830, 831, 1442.

140. Some limited partners in Respondent PPCL requested Respondent Hanlester to return the purchase price of their shares to them. Tr. at 1563 -1564, 1794 - 1795.

141. The I.G. did not prove that the reason that Respondent Hanlester returned the purchase price of shares to some limited partners in Respondent PPCL was their failure to refer sufficient business to a joint venture laboratory. Tr. at 2020, 2217; see Tr. at 542 - 545; 1460 - 1461, 1490, 1528 - 1529, 1563 - 1564, 1794 - 1795, 1841; see Findings 133 - 137.

142. The I.G. did not prove that Respondent Lewand, Respondent Tasha, or Respondent Welsh directed Respondent Hanlester to return the purchase price of shares to some limited partners in Respondent PPCL because of the partners' failure to refer sufficient business to a joint venture laboratory. See Findings 133 - 137.

143. On April 9, 1987, Respondent Hanlester and SKBL entered into a master laboratory services agreement. I.G. Ex. 1.0.

144. In the master laboratory services agreement, Respondent Hanlester agreed to offer SKBL the opportunity to provide management services for joint venture laboratories organized by Respondent Hanlester. I.G. Ex. 1.0/2.

145. In the master laboratory services agreement, SKBL agreed to provide laboratory management services to all joint venture laboratories in which Respondent Hanlester had an ownership interest. I.G. Ex. 1.0/3.

146. On July 27, 1987, SKBL entered into a laboratory management agreement with Respondent PPCL. I.G. Ex. 4.1.

147. The laboratory management agreement required Respondent PPCL to provide facilities and equipment necessary for appropriate operation of the laboratory. I.G. Ex. 4.1/2.

148. The laboratory management agreement required Respondent PPCL to provide the services of a licensed medical director. I.G. Ex. 4.1/3.

149. The laboratory management agreement required Respondent PPCL to repair and maintain laboratory space and to pay utility charges incurred by the laboratory. I.G. Ex. 4.1/3.

150. The laboratory management agreement required SKBL to provide and compensate all staff necessary to operate the laboratory. I.G. Ex. 4.1/3.

151. The laboratory management agreement required SKBL to supervise the administrative and operational activities of the laboratory. I.G. Ex. 4.1/3 - 4.

152. The laboratory management agreement required SKBL to provide all necessary equipment not already provided by Respondent PPCL, and to maintain and repair all laboratory equipment. I.G. Ex. 4.1/4.

153. The laboratory management agreement required SKBL to conduct all billing and collection activities for the laboratory. I.G. Ex. 4.1/5.

154. The laboratory management agreement required Respondent PPCL to pay SKBL a monthly management fee of $15,000.00 or 80 percent of all net cash receipts, whichever was greater. I.G. Ex. 4.1/5 - 6.

155. Subsequent to July 27, 1987, Respondent Hanlester, Respondent PPCL and SKBL agreed to reduce PPCL's monthly management fee to SKBL under the laboratory management agreement to $15,000.00 or 76 percent of all net cash receipts, whichever was greater. I.G. Ex. 4.3; Tr. at 410, 2011 - 2012, see Finding 146.

156. On July 27, 1987, Respondent Hanlester and SKBL entered into a laboratory support services agreement. I.G. Ex. 4.2.

157. Respondent Hanlester and SKBL agreed that Respondent Hanlester would be responsible for setting up, maintaining, and servicing the client accounts for Respondent PPCL. I.G. Ex. 4.2/2 - 3.

158. Respondent Hanlester and SKBL agreed that, as compensation for setting up, maintaining, and servicing the client accounts of Respondent PPCL, Respondent Hanlester would receive four percent of Respondent PPCL's net cash receipts. I.G. Ex. 4.2/12.

159. When Respondent Hanlester, Respondent PPCL, and SKBL agreed to reduce SKBL's management fee from 80 percent of Respondent PPCL's net cash receipts to 76 percent of Respondent PPCL's net cash receipts, they simultaneously agreed that Respondent Hanlester would not be paid the compensation agreed to in the laboratory support services agreement. I.G. Ex. 4.3/1.

160. In July, 1988, Respondent Hanlester, Respondent Omni, and SKBL agreed that SKBL would manage laboratory facilities for Respondent Omni. I.G. Ex. 5.1.

161. The terms and conditions pursuant to which SKBL would manage Respondent Omni's laboratory, the rights and duties of Respondent Hanlester, Respondent Omni, and SKBL, and the compensation to be paid to SKBL were basically the same as was provided in the agreements between Respondent Hanlester, Respondent PPCL, and SKBL. These terms and conditions included a monthly management fee of $15,000.00 or 76 percent of net cash receipts, whichever was greater. I.G. Ex. 5.1; <u>see</u> Findings 146 - 159.

162. In August, 1988, Respondent Hanlester, Respondent Placer, and SKBL agreed that SKBL would manage laboratory facilities for Respondent Placer. I.G. Ex. 6.1.

163. The terms and conditions pursuant to which SKBL would manage Respondent Placer's laboratory, the rights and duties of Respondent Hanlester, Respondent Placer, and SKBL, and the compensation to be paid to SKBL were basically the same as was provided in the agreements between Respondent Hanlester, Respondent PPCL, and SKBL. These terms and conditions included a monthly management fee of $15,000.00 or 76 percent of net cash

receipts, whichever was greater. I.G. Ex. 6.1; see Findings 146 - 159.

164. One effect of the agreements between Respondent Hanlester, Respondent PPCL, Respondent Omni, Respondent Placer, and SKBL, was to shift the operating risks of running the joint venture laboratories from Respondent Hanlester, Respondent PPCL, Respondent Omni, and Respondent Placer to SKBL. Findings 146 - 163.

165. The compensation that Respondents PPCL, Omni, and Placer paid to SKBL in return for SKBL's assumption of the operating risks of the joint venture laboratories was 76 percent of the joint venture laboratories' revenues, if greater than $15000.00. Findings 155, 161, 163.

166. The risk assumed by SKBL in this relationship was that its costs of managing the joint venture laboratories might exceed 76 percent of the laboratories' revenues. Findings 164, 165.

167. A risk assumed by Respondent Hanlester, Respondent PPCL, Respondent Omni, and Respondent Placer in this relationship was that SKBL would fail to efficiently manage the joint venture laboratories, thereby causing physicians to cease referring business to the laboratories. Tr. at 206 - 207, 210 - 212.

168. SKBL deposited the receipts earned by Respondent PPCL, Respondent Omni, and Respondent Placer in an account which was maintained for each of the aforesaid Respondents. Tr. at 625, 670, 673.

169. The accounts were maintained by SKBL pursuant to the agreements between Respondents Hanlester, PPCL, Omni, Placer, and SKBL. Tr. at 673; Findings 153, 160, 162.

170. Payments were made from these accounts to: make refunds to patients for overpayments or to correct billing errors; compensate Respondent Hanlester pursuant to the laboratory support services agreements; compensate SKBL for its management services; and compensate Respondent PPCL, Respondent Omni, and Respondent Placer. I.G. Ex. 40.0; Tr. at 625.

171. In October 1987, SKBL decided to make payments to Respondent PPCL based on expected collections from laboratory tests. I.G. Ex. 40.0, 41.0; Tr. at 626 - 629.

172. Expected collections exceeded that which actually had been collected. I.G. Ex. 40.0, 41.0; Tr. at 629.

173. SKBL treated the difference between what was paid based on expected collections and what actually had been collected as an advance to Respondent PPCL, to be deducted from future payments out of the account which SKBL managed on Respondent PPCL's behalf. I.G. Ex. 40.0, 41.0.

174. SKBL's purpose for advancing money to Respondent PPCL in 1987 was to provide greater initial compensation for Respondent PPCL's limited partners. Tr. at 628.

175. SKBL continued to make payments to Respondent PPCL based on expected collections until January 1990, when SKBL terminated its management agreement with Respondent PPCL. Tr. at 634.

176. SKBL made payments to Respondent Omni and to Respondent Placer based on expected collections. Tr. at 634 - 635.

177. SKBL's decision to make payments to Respondents PPCL, Omni, and Placer based on expected collections meant that these Respondents received distributions of revenue earlier than they otherwise would have. Tr. at 731, 732.

178. SKBL's decision to make payments to Respondents PPCL, Omni, and Placer based on expected collections did not mean that these Respondents received greater total distributions of revenue than they were entitled to receive under their management agreements with SKBL. _See_ Findings 171 - 177.

179. SKBL's decision to make payments to Respondents PPCL, Omni, and Placer based on expected collections enabled these Respondents to make distributions of revenue to their limited partners in the amounts distributed earlier than otherwise would have been possible. _See_ Finding 177.

180. SKBL's decision to make payments to Respondents PPCL, Omni, nd Placer based on expected collections did not mean that these Respondents were able to make greater total distributions of revenue to their limited partners than otherwise would have been possible. _See_ Finding 178.

181. SKBL elected to perform many of the laboratory tests sent to Respondent PPCL, Respondent Omni, or Respondent Placer at SKBL facilities. I.G. Ex. 38.0, 42.0, 43.0; Tr. at 636 - 640.

182. SKBL processed at its central processing laboratory in Van Nuys, California all of the tests sent to Respondent PPCL or to Respondent Omni and not performed by these Respondents' laboratories. Tr. at 344 - 345; 575 - 576.

183. SKBL processed at its central processing laboratory in Dublin, California, many of the tests sent to Respondent Placer and not performed by this Respondent's laboratory. Tr. at 575 - 576.

184. One reason that SKBL elected to process tests from Respondents PPCL, Omni, and Placer at its central processing facilities was that it was more efficient for SKBL to process tests centrally than at these Respondents' laboratories. Tr. at 434.

185. It is not uncommon for small clinical laboratories to refer laboratory tests to larger laboratories in order to benefit from the more efficient processing which may be provided by larger laboratories. Tr. at 191, 384 - 385; see Tr. at 1384.

186. It was to SKBL's advantage under its management agreements with Respondents PPCL, Omni, and Placer to process laboratory tests as efficiently and economically as possible. Findings 165, 166.

187. Respondents PPCL, Omni, and Placer did not maintain sufficient equipment at their laboratories to conduct all tests sent to them at these laboratories. Tr. at 434.

188. Respondents PPCL, Omni, and Placer maintained sufficient equipment at their laboratories to perform "stat tests" -- meaning tests ordered by physicians that required immediate results. Tr. at 435 - 436.

189. Such stat tests included pregnancy tests and tests to monitor blood levels of medications. Tr. at 435 - 436.

190. The percentage of tests that physicians sent to Respondents PPCL, Omni, or Placer which were performed at these Respondents' laboratories ranged from about 10 to about 15 percent. Tr. at 438.

191. Most of the laboratory tests sent to Respondents PPCL, Omni, and Placer were sent by physicians who were limited partners in these Respondents. I.G. Ex. 92.2, 93.1, 94.1.

192. Most of the laboratory tests sent to Respondents PPCL, Omni, and Placer by physicians who were not limited partners in these Respondents were sent by physicians whose practices were located within a short distance from the laboratories operated by Respondents PPCL, Omni, and Placer. Tr. at 897, 933 - 934.

193. Most of the revenues earned by Respondents PPCL, Omni, and Placer were earned from tests sent to these Respondents by limited partners. See Finding 191.

194. Respondents PPCL, Omni, and Placer could not have been profitable unless limited partners sent a substantial number of laboratory tests to them. See Findings 191, 193.

195. Respondents PPCL, Omni, and Placer made distributions to each of their limited partners based on net profits and the amount of limited partnership shares owned by each partner. Tr. at 1234, 2100; Finding 48.

196. Respondents PPCL, Omni, and Placer did not make distributions to any of their limited partners based on the amount of tests sent to a joint venture laboratory by that partner. Tr. at 227, 1234; Finding 48.

197. Respondent PPCL paid its limited partners returns on their investments of about 18 percent in 1987, 65 percent in 1988, and 60 percent in 1989. I.G. Ex. 27.0; Tr. at 1208.

198. Respondent Omni paid its limited partners a return on their investment of about 50 percent in 1989. See I.G. Ex. 22.1, 32.0, 86.0.

199. Respondent Placer paid its limited partners a return on their investment of more than 50 percent in 1989. See I.G. Ex. 23.1, 32.0, 86.2.

200. The I.G. did not prove that the rates of return which Respondent PPCL, Respondent Omni, or Respondent Placer paid to their limited partners greatly exceeded that which is typically paid by health care limited partnerships to their limited partners. See Findings 195 - 197.

201. The I.G. did not prove that SKBL's assumption of the risk of operating laboratories owned by Respondents PPCL, Placer, and Omni constituted payment of remuneration to these Respondents and Respondent Hanlester in return for their referring laboratory tests to SKBL. See Findings 164 - 166.

202. The I.G. did not prove that SKBL's decision to make distributions to Respondents PPCL, Omni, and Placer based on expected collections of revenues rather than on actual collections constituted payment of remuneration to these Respondents and Respondent Hanlester in return for their referring laboratory tests to SKBL. See Findings 171 - 180.

203. The I.G. did not prove that the management relationship between Respondents Hanlester, PPCL, Omni, and Placer, and SKBL eliminated virtually all risk to limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer. See Findings 56 - 60, 167.

204. The I.G. did not prove that the management relationship between Respondents Hanlester, PPCL, Omni, and Placer, and SKBL was intended by Respondents to disguise remuneration from SKBL to Respondents Hanlester, PPCL, Omni, and Placer in return for these Respondents' referring laboratory tests to SKBL. See Findings 143 - 186.

205. The I.G. did not prove that Respondents Lewand, Tasha, Welsh, Huntsinger, Hanlester, Keorle, PPCL, Omni, or Placer solicited or received remuneration from SKBL in return for referring Medicare or Medicaid business to SKBL. See Findings 143 - 186.

206. The I.G. did not prove that Respondents Lewand, Tasha, Welsh, Huntsinger, or Keorle offered physicians the opportunity to buy limited partnership shares in Respondents PPCL, Omni or Placer conditioned on these physicians agreeing to send laboratory tests to joint venture laboratories. See Findings 33 -66, 73 - 89, 99 - 106.

207. The I.G. did not prove that Respondents Lewand, Tasha, Welsh, Huntsinger, or Keorle offered physicians the opportunity to buy limited partnership shares in Respondents PPCL, Omni, or Placer in amounts determined by or related to the business that these physicians were willing to send to joint venture laboratories. See Findings 33 - 66, 73 - 89, 99 - 106.

208. The I.G. did not prove that Respondents Lewand, Tasha, Welsh, Huntsinger, Hanlester, Keorle, PPCL, Omni, or Placer conditioned continuing ownership of limited partnership shares in Respondents PPCL, Omni, or Placer on limited partners sending tests to joint venture laboratories. See Findings 119 - 142.

209. The I.G. did not prove that Respondents Lewand, Tasha, Welsh, Huntsinger, Hanlester, Keorle, PPCL, Omni, or Placer disguised payments to limited partners for tests referred to joint venture laboratories as partnership distributions on investments. See Findings 193 - 200.

210. The I.G. did not prove that Respondents Lewand, Tasha, Welsh, Huntsinger, Hanlester, Keorle, PPCL, Omni, or Placer offered or paid compensation to physicians in return for their agreeing to send tests to joint venture laboratories. Findings 206 - 208.

211. The I.G. proved that Ms. Hitchcock, acting as the agent of Respondents Hanlester, PPCL, Omni, and Placer knowingly and willfully offered physicians the opportunity to buy limited partnership shares in Respondents PPCL, Omni, and Placer conditioned on these physicians agreeing to send laboratory tests to joint venture laboratories. Findings 67 -72, 90 - 98.

212. The I.G. proved that Ms. Hitchcock, acting as the agent of Respondents Hanlester, PPCL, Omni, and Placer knowingly and willfully offered physicians the opportunity to buy limited partnership shares in Respondents PPCL, Omni, and Placer based on the volume of business that these physicians were anticipated to send to joint venture laboratories. Findings 67 - 72, 90 - 98.

213. The I.G. proved that Ms. Hitchcock, acting as the agent of Respondents Hanlester, PPCL, Omni, and Placer knowingly and willfully conditioned continuing ownership of limited partnership shares in Respondents PPCL, Omni, and Placer on limited partners sending tests to joint venture laboratories. Findings 67 - 72, 90 - 98.

214. The I.G. did not prove that Ms. Hitchcock acted as the agent of Respondents Lewand, Tasha, Welsh, Huntsinger, or Keorle. See Findings 67 - 72, 99 - 106.

215. The Secretary of the Department of Health and Human Services (the Secretary) has the authority to exclude from participation in Medicare and Medicaid any individual or entity whom he has determined has committed an act described in Section 1128B of the Act. Social Security Act, section 1128(b)(7).

216. The Secretary delegated to the I.G. the authority to propose exclusions pursuant to section 1128(b)(7) of the Act. See 48 Fed. Reg. 21662, May 13, 1983.

217. Section 1128B(b)(1) of the Act prohibits a party from knowingly and willfully soliciting or receiving any payment in return for referring items or services which are compensated for by Medicare or Medicaid. Social Security Act, section 1128B(b)(1).

218. Section 1128B(b)(2) of the Act prohibits a party from knowingly and willfully offering or making any payment to obtain an agreement to refer, or referral of, items or services which are compensated for by Medicare or Medicaid. Social Security Act, section 1128B(b)(2).

219. In order to violate section 1128B(b)(2) of the Act, a party must knowingly and willfully offer to make a payment conditioned on the offeree agreeing to refer items or services which are compensated for by Medicare or Medicaid. Social Security Act, section 1128B(b)(2).

220. Under section 1128B, a principal is liable for the acts of an agent which are committed on the principal's behalf, even if the principal did not authorize the agent to commit such acts. Social Security Act, section 1128B.

221. The I.G. did not prove that Respondents Lewand, Tasha, Welsh, Huntsinger, Hanlester, Keorle, PPCL, Omni, or Placer knowingly and willfully solicited or received remuneration to refer items or services which are compensated for by Medicare or Medicaid, in violation of section 1128B(b)(1) of the Act. See Finding 205.

222. By virtue of the acts of their agent Ms. Hitchcock, Respondents Hanlester, PPCL, Omni, and Placer knowingly and willfully offered remuneration to physicians to induce them to refer items or services which are compensated for by Medicare or Medicaid, in violation of section 1128B(b)(2) of the Act. Findings 210 - 212, 219.

223. The I.G. did not prove that Respondents Lewand, Tasha, Welsh, Huntsinger, or Keorle knowingly and willfully offered or paid remuneration to physicians to induce them to refer items or services which are compensated for by Medicare or Medicaid, in violation of section 1128B(b)(2) of the Act. See Findings 205 - 211.

224. The remedial purpose of an exclusion pursuant to section 1128 of the Act is to protect federally-funded health care programs and their beneficiaries and recipients from individuals and entities who have been shown to be untrustworthy. Social Security Act, section 1128.

225. An ancillary purpose of an exclusion pursuant to section 1128 of the Act is to deter individuals and entities from engaging in conduct which jeopardizes the integrity of federally-funded health care programs, or the welfare of beneficiaries and recipients of these programs. Social Security Act, section 1128.

226. The I.G. did not prove that Respondents Hanlester, PPCL, Omni, or Placer continue to be an untrustworthy entities, or that they continue to jeopardize the integrity of federally-funded health care programs, or the welfare of beneficiaries and recipients of these programs. See Finding 107.

227. In this case no exclusion is reasonably needed to satisfy the remedial purpose of section 1128 of the Act. Social Security Act, section 1128.

ANALYSIS

I. The parties' contentions

A. The I.G.'s contentions

The I.G. argues that Respondents violated the Act in two respects. First, Respondents, in marketing joint venture limited partnerships to individual physicians, allegedly offered or paid remuneration to these physicians in violation of section 1128B(b)(2) of the Act. This section sanctions a party who:

> (K)nowingly and willfully offers or pays any remuneration (including any kickback, bribe, or rebate) directly or indirectly, overtly or covertly, in cash or in kind to any person to induce such person --

(A) to refer an individual to a person for the furnishing of any item or service for which payment may be made in whole or in part under title XVIII or a State health care program, or

(B) to purchase, lease, order, or arrange for or recommend purchasing, leasing, or ordering any good, facility, service, or item for which payment may be made in whole or in part under title XVIII or a State health care program . . . .

Second, Respondents allegedly solicited or received remuneration from SKBL in violation of section 1128B(b)(1) of the Act. This section sanctions a party who:

> (K)nowingly and willfully solicits or receives any remuneration (including any kickback, bribe, or rebate) directly or indirectly, overtly or covertly, in cash or in kind --
>
> (A) in return for referring an individual to a person for the furnishing or arranging for the furnishing of any item or service for which payment may be made in whole or in part under title XVIII or a State health care program, or
>
> (B) in return for purchasing, leasing, ordering, or arranging for or recommending purchasing, leasing, or ordering any good, facility, service, or item for which payment may be made in whole or in part under title XVIII or a State health care program . . . .

1. <u>The I.G.'s contentions concerning the relationship between Respondents and limited partners in the three joint venture laboratories</u>

The I.G. contends that the Respondents violated section 1128B(b)(2) of the Act because they offered and paid "remuneration" to individual physicians to "induce" those physicians to refer Medicare business to the joint venture laboratories. The allegedly unlawful inducement consisted of the opportunity to own shares in the laboratories and to share in the laboratories' profits where, according to the I.G., the partners were "virtually guaranteed" a high rate of return on their investments, so long as they referred laboratory tests to the joint ventures.

The I.G. asserts that Respondents conditioned limited partners' purchase of joint venture shares on the partners' agreement to refer laboratory tests to the joint venture laboratories. According to the I.G., physicians were permitted to purchase limited partnership shares based on the number of laboratory tests they were likely to refer. The I.G. contends that potential purchasers of limited partnership interests were told that their participation was conditioned on their agreement to refer tests to the joint venture laboratories. The I.G. also argues that physicians who failed to live up to this agreement were ousted from ownership and their share purchase money was returned to them.

The I.G. also asserts that Respondents violated the Act even if they did not condition the offers to sell partnership shares on the requirement that physicians who purchased shares in the joint venture laboratories refer tests to those laboratories. He contends that Respondents violated the Act simply by encouraging physicians to refer tests to the joint venture laboratories through offers of low risk equity shares and high rates of return on investments. He asserts that under the Act the gravamen of the fraud is the act of inducement. The inducement is illegal, according to the I.G., even if Respondents did not require as a quid pro quo to physicians' purchasing shares that they agree to refer tests to the joint venture laboratories.

The I.G. does not contend that all joint ventures among health care providers violate the Act. The I.G. contends that the remuneration scheme of these joint ventures is illegal, because the remuneration offered and given to the limited partners was not a legitimate return on an investment. The fraudulent inducement allegedly lies in the artificially low risks and artificially high returns which the I.G. contends Respondents offered to physicians in order to attract their participation and their referrals of laboratory tests. The investment arrangement in this case allegedly was an artifice intended to channel payments to physicians in order to induce them to refer laboratory tests to the joint venture laboratories.

The I.G. asserts that several features of the joint ventures establish his contention that the investment arrangement was merely an artifice. These include: (1) targeting of certain physicians, either by specialty or by geographic location, as likely purchasers of investment shares; (2) monitoring referrals to the joint venture laboratories by individual physician investors; (3) payment to investors of virtually guaranteed high rates of return on their investments; and (4) dependence of the joint venture laboratories on limited partners' test referrals as a primary source of revenues.

Indeed, according to the I.G., there was no purpose to the Respondents' raising investment capital from physician investors other than to disguise the true purpose of the joint ventures, which was to induce laboratory referrals. The I.G. contends that there was little or no need for Respondents to raise money from investors, inasmuch as operating costs were allegedly assumed by SKBL as an element of its management contracts with the joint venture laboratories.

2. <u>The I.G.'s contentions concerning the relationship between the laboratories and SKBL</u>

The I.G. argues that the business relationship between the joint venture laboratories and SKBL constitutes unlawful solicitation and receipt of remuneration by Respondents under section 1128B(b)(1). He asserts that the evidence proves that SKBL made payments to Respondents in order to capture the laboratory tests referred to the joint venture laboratories by limited partner physicians.

The I.G. contends that the management agreements between these laboratories and SKBL were artifices which enabled SKBL to pay Respondents for referral of laboratory tests from the joint venture laboratories to SKBL. The management agreements specified that the laboratories would pay SKBL a percentage of revenues from laboratory tests, in return for SKBL agreeing to assume management of the laboratories. The I.G. argues that SKBL did not manage the laboratories so much as it used them as mere conduits for tests to be performed by SKBL. The I.G. asserts that the joint venture laboratories in fact performed few tests. SKBL performed nearly all of the tests ordered from the laboratories at its own facilities. There allegedly was little capital invested in the joint venture laboratories' facilities and equipment and the laboratories had no employees, aside from Dr. Huntsinger, their medical director. The laboratories thus were, according to the I.G., merely conduits for tests and funds, and not viable clinical laboratories. Therefore, the percentage of the test revenues retained by the joint venture laboratories was not earnings by the laboratories on their business operations, according to the I.G. Rather, it constituted "indirect" remuneration unlawfully solicited by Respondents and paid by SKBL.

B. Respondents' contentions

Respondents reject both the I.G.'s factual and legal analysis. They deny that they unlawfully offered or paid remuneration to individual physicians and they deny that they unlawfully solicited or received any remuneration from SKBL.

1. Respondents' contentions concerning their relationship with individual investors in the three joint venture laboratories

Respondents argue that the I.G. mischaracterizes the facts of the case in order to conform them to his theory of illegality. Respondents contend that many of the features of the joint ventures identified by the I.G. as evidencing unlawful offers of or payment of remuneration to physician investors neither are accurately described by the I.G. nor support the I.G.'s contentions.

Respondents deny that they ever conditioned ownership of limited partnership interests in the laboratories on purchasers' promises to refer tests to the laboratories. They deny that partners were removed for failure to refer business. Respondents assert that many of the limited partners referred tests in amounts which were disproportionate to their ownership interests. They contend that some investors referred no tests and continued as partners, sharing in the revenues of the joint venture laboratories.

Respondents assert that the fact that physicians who were higher users of laboratory tests were sought as investors in the joint ventures is benign. They contend that this marketing strategy mirrors a common and logical practice in the health care field of seeking investors in joint ventures who will be likely users of the ventures' facilities. Respondents contend that their encouragement of investors to refer tests to the joint venture laboratories merely reflects the obvious fact that these laboratories needed referrals in order to survive. They deny that they offered prospective investors an unusually high rate of return on their investment or promised prospective investors that their investment would be virtually risk-free. Respondents aver that the limited partners incurred risks not atypical for limited partnership arrangements in the health care industry, as well as in other markets.

Respondents argue that no illegality results from their encouraging investors in the laboratories to refer laboratory tests to these laboratories because they did not require investors to refer tests as a condition for being permitted to invest in the laboratories. They assert that the Act proscribes the solicitation, entry into, and consummation of agreements to pay remuneration for referrals. Respondents assert that, to interpret the law as is argued by the I.G., would produce the absurd consequence of rendering illegal a myriad of benign or procompetitive business arrangements in the health care market. Assuming the I.G. elected not to prosecute all of these arrangements, he could nonetheless exercise virtual _carte blanche_ authority to pick and choose among them to attack those which he disliked. Respondents contend that reposing such unlimited discretion in the I.G. is inimical to Congressional intent.

2. _Respondents' contentions concerning the relationship between the laboratories and SKBL_

According to Respondents, the I.G. grossly mischaracterizes the relationship between the joint venture laboratories and SKBL in order to buttress his contention that Respondents unlawfully received remuneration from SKBL. Respondents argue that the laboratories entered into legitimate management agreements with SKBL. They contend that Respondents PPCL, Omni, and Placer compensated SKBL for its management services. No remuneration, direct or otherwise, was paid to the laboratories by SKBL.

Respondents dispute that the fact that most of the tests ordered from the joint venture laboratories were shipped to SKBL's facilities for completion establishes that the joint venture laboratories were shells or conduits, as is contended by the I.G. They contend that the pass-through of tests from smaller laboratories to larger, more sophisticated, laboratories is a common and benign practice. Furthermore, the decision to perform tests at SKBL facilities was, according to Respondents, an option legitimately exercised by SKBL as an aspect of its management contract with Respondents, and not as a subterfuge.

II. <u>Analysis of the Evidence</u>

I find that Respondents established Respondents PPCL, Omni, and Placer in order to profit from the laboratory tests which limited partner physicians ordered. In order to maximize profits, Respondents actively sought as limited partners those physicians who would be likely to refer large numbers of tests to joint venture laboratories. Respondents enticed physicians to become limited partners by offering them potentially lucrative investments. They gave limited partners the opportunity to profit from ordering tests that they could not otherwise profit from. Respondents encouraged limited partners to refer tests and warned limited partners of the dire consequences to the joint ventures of their failure to refer tests.

However, Respondents did not intend to condition ownership of limited partnership shares on physicians' agreeing to refer tests, nor did they intend to suggest to physicians that they must refer tests as a continuing condition of limited partnership. I do not find that Respondents disciplined limited partners who failed to refer tests in sufficient quantity, either by ousting them as limited partners or by threatening to oust them.

This analysis is in some respects complicated by the fact that, notwithstanding Respondents' intentions, Ms. Hitchcock, acting as agent for Respondents Hanlester, PPCL, Omni, and Placer, did represent to at least some physicians that a physician's eligibility for ownership of partnership shares would be related to the amount of business that that physician was willing to refer. Ms. Hitchcock also communicated to at least some physicians that limited partners who did not pull their weight in making referrals would be ousted from the partnerships. Although Respondents did not intend that Ms. Hitchcock make such communications (and, in fact, instructed Ms. Hitchcock not to make them), she nonetheless made them. Physicians who heard Ms. Hitchcock's sales presentations could have been led to believe that Ms. Hitchcock was asserting the policy of Respondents Hanlester, PPCL, Omni, and Placer.

I do not find that the laboratories established by Respondents PPCL, Omni, and Placer were sham operations established to disguise payments for referrals of laboratory tests from SKBL to Respondents, and, ultimately, to limited partners. Respondents' motives for the way in which they structured the operations of Respondents PPCL, Omni, and Placer can be explained as legitimate business objectives, having nothing to do with disguising payments.

Respondents entered into management agreements with SKBL that shifted the costs of operating the joint venture laboratories from Respondents PPCL, Omni, and Placer to SKBL. This was an advantage for Respondents, because it relieved them of the day-to-day burdens of laboratory management. The advantage would have obtained whether PPCL, Omni, and Placer were operated as joint venture laboratories or under some other form of ownership, such as single owner proprietorships. The management relationship also advantaged Respondents by enabling them to advertise Respondents PPCL, Omni, and Placer as high quality operations without having to incur the capital costs needed to duplicate that which SKBL was capable of providing.

Respondents paid SKBL substantial consideration for this management relationship. The relationship was advantageous to SKBL because it was potentially profitable, and because it potentially captured a stream of laboratory tests that would be ordered by limited partners. However, the evidence does not establish that SKBL made payments to Respondents in order to capture this stream of tests.

A. Respondents' relationships to each other

These cases involve the creation and operation of three limited partnerships, Respondents PPCL, Omni, and Placer. The structure, ownership, and operation of each of these partnerships was essentially identical. Each was a limited partnership organized under California law. Findings 16, 23, 29. These partnerships were organized to operate clinical laboratories to serve defined communities within California. Findings 17, 24, 30. The general partner of Respondent PPCL, Respondent Omni, and Respondent Placer was Respondent Hanlester, which was also a California partnership. Findings 4, 18, 25, 31.

The limited partners in Respondents PPCL, Omni, and Placer essentially consisted of physicians who purchased shares in these Respondents. The limited partners each had potential liability equivalent to the value of their respective partnership shareholdings. All management decisions for the limited partnerships were made by the general partner, Respondent Hanlester. Findings 19, 26, 32.

Respondent Hanlester originally had several general partners. These included Respondents Tasha and Welsh. Finding 6. Respondent Welsh ceased being a general partner or executive in Respondent Hanlester in the summer of 1987. Finding 12. The majority interest in Respondent Hanlester was originally owned by Hanlester Corporation, a California corporation whose shareholders included Respondent Lewand. Findings 2, 3, 7. In January 1989, Hanlester Corporation sold its majority interest in Respondent Hanlester to Respondent Tasha. Subsequently, Hanlester Corporation changed its name to Keorle Corporation (Respondent Keorle). Findings 2, 3, 8.

Respondents Lewand, Tasha, and Welsh each served for a time as executives in Respondent Hanlester. Until his Summer, 1987 departure, Respondent Welsh was Respondent Hanlester's Vice-President for Business Development. Finding 11. Respondent Tasha was Vice-President for Operations. Finding 10. Respondent Lewand was President of Respondent Hanlester until January 1989. Finding 9.

Respondent Huntsinger was neither an officer, a general partner, nor an employee of Respondent Hanlester. Although he was listed in one of Respondent Hanlester's sales brochures as Respondent Hanlester's medical director, he did not serve in any management or executive capacity with this Respondent. Respondent Huntsinger contracted with SKBL to serve as medical director of Respondents PPCL and Omni. Finding 114.[3] However, Respondent Huntsinger did own a substantial limited partnership interest in Respondent PPCL. Finding 20.

B. <u>Respondents' plans for establishing Respondents PPCL, Omni, and Placer and for marketing limited partnership shares</u>

Respondents offered potentially lucrative investments to physicians in order to encourage them to become limited partners in Respondents PPCL, Omni and Placer, and to refer laboratory tests to joint venture laboratories. Respondents urged potential limited partners to refer tests by telling them that such referrals were a <u>sine</u> <u>qua</u> <u>non</u> for the laboratories' success. Respondents did not intend to condition ownership of limited partnership shares on physicians'

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[3] SKBL's relationship to Respondents is discussed in detail, <u>infra.</u> <u>See</u> Findings 143 - 186, 201, 202, 204.

agreeing to refer business. Respondents did not intend to link the number of limited partnership shares that a physician could own to the amount of business that the physician could refer.

Respondents' intent in creating Respondents PPCL, Omni, and Placer is evident in the private placement memoranda which they distributed to prospective limited partners. Respondents' objective was to create entities which could be marketed to physicians as attractive investments which would generate income for Respondents and for the physicians who purchased limited partnership shares. The key to this strategem was that physician investors would refer laboratory tests to the joint ventures' laboratories.

Respondents' strategy for marketing joint venture shares focused on enlisting as limited partners those physicians who could potentially refer large numbers of tests to joint venture laboratories. Findings 80, 81. As Respondents noted in their private placement memoranda, the joint ventures' laboratories would initially generate substantially all revenues from tests ordered by limited partners. Finding 42. The laboratories would always depend on limited partners' referrals as their primary source of business. Id.

Respondents sought to make limited partnership investments attractive to physicians through a number of inducements. Respondents offered partnership shares at a relatively low price ($500 per share) and in small minimum quantities per investor (the minimum required purchase was three shares). The minimum limited partnership investment in Respondents PPCL, Omni, and Placer therefore was $1500. Findings 34 - 38. Respondents told potential investors that, assuming the joint ventures succeeded in attracting significant numbers of limited partners and referred tests, they could earn relatively high rates of return on their investments. Possible annual rates of return of 50 percent or greater were advertised to potential limited partners. Finding 53.

Another significant inducement offered by Respondents to potential limited partners to invest in Respondents PPCL, Omni, and Placer was that the investments enabled physicians to earn income indirectly from referred laboratory tests where they were legally barred from earning income directly from those tests. In 1984, Congress enacted legislation which provided that Medicare would compensate only the party which actually performs or supervises the performance of a clinical laboratory test. Social Security Act, section 1833(h)(5)(A).[4] This provision effectively barred physicians from claiming reimbursement from Medicare for tests which they ordered, but which they did not personally perform or supervise. However, as equitable owners in Respondents PPCL, Omni, or Placer, physicians could indirectly earn reimbursement for Medicare-reimbursed laboratory tests in the form of partnership distributions based on the joint ventures' profits. As one of the limited partners in Respondent PPCL testified:

> [A]t that time Medicare was changing their regulations wherein the doctor couldn't charge a drawing, handling and interpretation fee in addition to lab work, which is how we usually bill lab work to other people . . . . When Medicare came forward with that regulation, that obviously indicated an income loss for me, and this was a way to help recoup some of that.

Tr. at 1452 - 1453.

Respondents also suggested to potential limited partners that the joint ventures would be affiliated with SKBL, an entity with a national reputation in the clinical laboratory business. Findings 61, 62. SKBL's reputation for quality and success was a strong inducement for physicians to invest in the joint ventures.

The evidence does not establish the I.G.'s contention that Respondents intended to induce physicians to buy partnership shares in Respondents PPCL, Omni, or Placer by guaranteeing their investments or by assuring physicians that their investments would be virtually risk-free. To the contrary, the private placement memoranda which Respondents provided to potential limited partners contained extensive recitations of the potential risks of investment. Findings 54 - 60. Respondents told potential limited partners that investment in Respondents PPCL, Omni, or Placer involved a high degree of risk. Finding 56. Potential limited partners were told not to invest unless they

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[4] The exception to this law was the situation where a laboratory referred a test to another laboratory. In that case, either the laboratory which performed the test or the laboratory which referred it was permitted to claim reimbursement from Medicare. Social Security Act, section 1833(h)(5)(A)(ii).

could afford a total loss of their investment. Finding 57.

The marketing strategy which Respondents developed to sell limited partnerships drew a line between urging prospective partners to consider buying into an entity which would generate profits based on tests that limited partners referred, and telling prospective partners that they would be required to refer tests as a condition for investment. The distinction which Respondents drew between exhorting partners to refer tests and requiring that they refer tests was neither faint nor subtle. On the one hand, physicians were told that it was in their economic self-interest to refer tests to joint venture laboratories. Respondents drove that point home by telling prospective limited partners that it would be a "blueprint for failure" of the joint ventures if partners did not refer tests to joint venture laboratories. I.G. Ex. 2.0; I.G. Ex. 3.0; Finding 44.

On the other hand, Respondents told prospective limited partners that their decision whether or not to patronize joint venture laboratories was voluntary. Finding 45. They told physicians that, under California law, it would be illegal to offer or pay consideration to a physician to induce or compensate that physician to refer patients to a laboratory. Finding 47. They told prospective limited partners their individual earnings from the joint ventures would not be based on the business they referred to joint venture laboratories. Finding 48. Respondents also stressed that, under California law, the joint ventures would be legal if "the physician's return on his or her investment in the limited partnership is not measured by the number or value of his or her referrals." I.G. Ex. 2.0/5.

I am convinced that Respondents intended to preserve this distinction between encouraging prospective limited partners to refer business and requiring that they do so as a condition for investment. Both Respondent Lewand and Mr. Aprahamian, the attorney who drafted the private placement memoranda, advised individual Respondents and Ms. Hitchcock that, in marketing limited partnership shares, no representations could be made to potential limited partners beyond that which was contained in the private placement memoranda. Findings 64 - 67, 73 - 79.[5]. The evidence does not show that either Respondents Lewand, Tasha, Welsh, or Huntsinger told prospective limited partners in Respondents PPCL, Omni, or Placer that as a condition of participation they would have to agree to refer laboratory tests to joint venture laboratories. Nor is there evidence which proves that Respondents intended to condition the number of shares a limited partner could own on the amount of business that the partner was in a position to refer to a joint venture laboratory. Respondents were told by Mr. Aprahamian that they could not condition the number of shares offered to a physician on that physician's anticipated referrals. Finding 79. Individual Respondents credibly denied making such a statement to any prospective limited partners. Finding 110.

The I.G. argues that a letter signed by Respondent Lewand evidences his and other Respondents' intent to condition ownership of shares on limited partners' agreement to refer business. I.G. Ex. 73.0. In this letter, Respondent Lewand represented to a physician that Respondent PPCL would extend to the physician's medical partnership the right of first refusal to purchase the remaining 30 limited partnership shares in Respondent PPCL contingent on the "full participation" of the medical partnership in Respondent PPCL. The I.G. contends that this language means that Respondent Lewand required the medical partnership to guarantee referral of all of its laboratory tests to Respondent PPCL as a condition for purchase of the remaining shares. Respondent Lewand contended in his testimony that the language simply meant that all of the members of the partnership would be offered the right to own shares. Tr. at 2024T - 2024V.

The term "full participation" in the letter is ambiguous and could reasonably be interpreted as either the I.G. or Respondent Lewand contend. The I.G. did not offer evidence to show that, in fact, any of the members of the medical partnership did refer all of their laboratory tests to Respondent PPCL subsequent to purchasing shares in that Respondent. Absent such evidence, and given the ambiguity of the letter, I do not find that it proves that Respondent Lewand conditioned the sale of the remaining shares in

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[5] I find that both Respondents Lewand and Mr. Aprahamian were credible witnesses.

Respondent PPCL on prospective partners agreeing to refer tests to Respondent PPCL.

C. Ms. Hitchcock's marketing activities

Although Respondents may have been careful to delineate between encouraging potential limited partners to refer business to joint venture laboratories and demanding that they do so, Ms. Hitchcock was not. The I.G. proved that Ms. Hitchcock told prospective limited partners in her capacity as Respondent Hanlester's Vice President of Marketing that the number of shares that limited partners could buy would depend on the amount of business that they were in a position to refer. Ms. Hitchcock also told prospective limited partners that if they purchased shares but then failed to refer business to joint venture laboratories pressure would be exerted against them either to increase their referrals or exit the joint ventures.

The I.G. urges that I find Ms. Hitchcock's representations to be part and parcel of Respondents' marketing and operating plans for Respondents PPCL, Omni, and Placer. If I were to agree with the I.G., it would follow that Respondents conditioned the sale of limited partnership shares in Respondents PPCL, Omni, and Placer on limited partners agreeing to refer tests to joint venture laboratories. The I.G. did not prove this contention. The weight of the evidence is that Ms. Hitchcock pursued a personal agenda in marketing joint venture shares to prospective limited partners. Actions taken by Ms. Hitchcock on the apparent authority of Respondents Hanlester, PPCL, Omni, and Placer were not always authorized by Respondents and were at times inimical to their interests.

Much of the I.G.'s evidence as to what Ms. Hitchcock told prospective limited partners consists of recordings of sales presentations which Ms. Hitchcock made to physicians in Las Vegas, Nevada. See I.G. Ex. 109; I.G. Ex. 110. These are not recordings of presentations made to potential limited partners in Respondents Hanlester, Omni, and Placer, and Respondents objected to my receiving them in evidence. However, Ms. Hitchcock testified that the recorded presentations were similar to the presentations that she normally gave. Tr. at 1121 - 1122. In light of this testimony, I find Ms. Hitchcock's recorded sales presentations to be illustrative of the sales presentations which she made to prospective limited partners in Respondents PPCL, Omni, and Placer.

Ms. Hitchcock did not directly state to prospective limited partners that they must agree to refer business to joint venture laboratories as a condition for purchasing limited partnership shares. Finding 97. However, the implication of her presentation was that the sale of shares was conditioned on the limited partners agreeing to refer business. She communicated this condition in two ways. First, Ms. Hitchcock told prospective limited partners that an "off the record" condition for the sale of shares was that the number of shares sold to a limited partner would be based on the anticipated volume of business that the partner would agree to refer to a joint venture laboratory. Finding 96.[6] Second, Ms. Hitchcock told prospective limited partners that those who did not refer business would be pressured to either increase their referrals or to sell back their shares to Respondent Hanlester. Finding 98.

Ms. Hitchcock made other representations to prospective limited partners that were at variance with what Respondents intended to communicate. For example, Ms. Hitchcock told prospective limited partners that the return on their investment in limited partnership shares virtually would be guaranteed. Finding 95. She also told prospective limited partners that they could anticipate annual returns on their investments of 300 percent or more. Finding 94.

Respondents found it difficult to control Ms. Hitchcock. Ms. Hitchcock testified that she had a personality conflict with Respondent Tasha. Tr. at 944. Respondent Lewand testified that in the Spring of 1988, Respondent Tasha concluded that Ms. Hitchcock was not controllable. Tr. at 2024J. Respondent Lewand attempted to personally manage Ms. Hitchcock as an alternative to discharging her. Id. By November, 1988, Respondent Lewand concluded that he had no choice but to terminate Ms. Hitchcock's employment. Tr. at 2024O.

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[6] In one memorandum, Ms. Hitchcock reiterated to a physician that she had offered "each physician . . . (apparently members of that physician's group practice) 3 units with the exception that all pathology come to the lab also - in that case I could probably sell you up to 5 units each." I.G. Ex. 72.4. There is no evidence that Ms. Hitchcock showed this memorandum to any of Respondents.

Ms. Hitchcock testified that she had been told by Respondent Lewand that the only information she could provide potential limited partners in her sales presentations was that which was contained in private placement memoranda. Finding 76. Respondent Lewand testified that he had given this directive to Ms. Hitchcock. Id. Mr. Aprahamian testified that, on several occasions, he counseled Ms. Hitchcock not to make representations beyond those which were contained in the private placement memoranda. Findings 73 - 76, 79. Similar instructions were communicated to Ms. Hitchcock by Respondents Tasha and Welsh. Finding 78. Therefore, what Ms. Hitchcock told limited partners not only departed from Respondents' private placement memoranda, it departed from the instructions which Respondents gave her as to what she could represent.

Ms. Hitchcock personally stood to gain from making unauthorized representations to prospective limited partners. Part of Ms. Hitchcock's compensation from Respondent Hanlester consisted of commissions on limited partnership shares that she sold. Finding 71. It was in her interest to make grandiose representations concerning possible profits if such representations operated to convince physicians to purchase limited partnership shares. It was also in her interest to convince physicians that they must refer business to joint venture laboratories as a condition for participation in a limited partnership, because another part of Ms. Hitchcock's compensation consisted of a percentage of the dollar volume of tests that physicians referred to the laboratories. Id.

There is additional evidence that Ms. Hitchcock operated in a manner which contradicted the interests and directives of Respondents. The I.G. contends that, as an element of the unlawful inducement of physicians to refer laboratory tests to joint venture laboratories, Respondent Lewand loaned money to physicians so that they could buy shares on favorable terms. Respondent Lewand did loan the purchase price for shares to three physicians. Finding 116. However, there is another, more plausible, explanation for these loans than the one offered by the I.G. Respondent Lewand testified credibly that, unbeknownst to him, Ms. Hitchcock had promised some physicians that Respondent Hanlester would loan them the purchase price of their shares. He made the loans in order to protect Respondent Hanlester's reputation in light of the promises that Ms. Hitchcock had made. Finding 118.

The foregoing is ample and convincing evidence that Respondents did not authorize Ms. Hitchcock's representations to physicians conditioning the purchase of joint venture shares on their agreement to refer laboratory tests. I am further persuaded that Ms. Hitchcock was acting in an unauthorized way by the fact that, given the marketing materials which Respondents published, it would have been foolhardy for them to suggest to physicians that the purchase of joint venture shares was conditioned on their agreement to refer business to joint venture laboratories. The private placement memoranda as much as told physicians that such requirement would violate California law. Finding 47.

However, Ms. Hitchcock led physicians to believe that she was acting on the authority of Respondents Hanlester, PPCL, Omni, and Placer. Her credibility with these physicians was buttressed by Respondent Hanlester's sales materials, which described her as one of the "Hanlester principals." I.G. Ex. 3.0. This material further described her as Respondent Hanlester's Vice President of Marketing. Id. Although Ms. Hitchcock served in no official capacity with Respondents PPCL, Omni, or Placer, she represented herself to physicians as the agent of these entities. Finding 92. Several physicians testified that they relied on or were persuaded by Ms. Hitchcock's sales representations. Prospective limited partners in Respondents PPCL, Omni, and Placer could reasonably believe that Ms. Hitchcock was acting on the authority of Respondents Hanlester, PPCL, Omni, and Placer. They could assume that she was telling the truth when she told them that referral of business was a condition of owning limited partnership shares.

D. Respondents' relationships with limited partners

According to the I.G., Respondents conditioned limited partners' ownership of shares on their ordering tests from joint venture laboratories. The I.G. argues that Respondents pressured physicians who became limited partners into ordering tests from joint venture laboratories. He asserts that Respondents ousted from the joint ventures those physicians who failed to order sufficient numbers of tests. He also contends that Respondents induced limited partners to continue to refer tests to joint venture laboratories by paying them high rates of return on their investments.

Much of the evidence offered by the I.G. to establish his contention that Respondents disciplined limited partners who failed to order sufficient amounts of tests consists of testimony by former limited partners concerning telephone conversations that they had with Respondent Huntsinger and events which transpired shortly after these conversations took place. The I.G. established that there were telephone conversations between Respondent Huntsinger and some limited partners in which Respondent Huntsinger pressured these physicians to increase the number of tests they ordered from joint venture laboratories. Respondents returned partnership investments to a few physicians, usually after they had engaged in conversations with Respondent Huntsinger.

Three of the physicians whom the I.G. called to testify about their telephone conversations with Respondent Huntsinger testified that, shortly after such conversations, they received unsolicited refunds of their limited partnership investments from Respondent Hanlester. These physicians, Drs. Rubin, Luster, and Saraf, testified to having had unpleasant conversations with Respondent Huntsinger prior to receiving refunds. See Tr. at 768, 1456. Several other physicians testified that, after conversations with Respondent Huntsinger which they described as annoying or unpleasant, they asked that their partnership investments be refunded to them, and Respondent Hanlester complied.

An inference arguably can be drawn that these witnesses were ousted from the joint ventures, from the witnesses' recitation of their conversations with Respondent Huntsinger and the subsequent refund of their partnership investments. However, that possible inference is rebutted in several respects. Based on the weight of the evidence, I conclude that the I.G. did not prove from the accounts of Dr. Huntsinger's telephone calls to physicians, including the conversations with Drs. Rubin, Luster, and Saraf, that Dr. Huntsinger called physicians in furtherance of a plan by Respondents to compel physicians to order laboratory tests as a condition of partnership. Nor did the I.G. prove that investments were refunded to some physicians because of their failure or unwillingness to order tests from joint venture laboratories.

The I.G. did not prove that Respondent Huntsinger ever threatened a limited partner with removal from a joint venture for failure to refer business. I have no doubt that, in his telephone conversations with limited partners, Respondent Huntsinger exhorted them to increase the business that they ordered from joint venture laboratories. Several physicians testified that Respondent Huntsinger persistently called them and asked them why they were not ordering more tests. Finding 127. It is apparent from these physicians' testimony that they found Respondent Huntsinger's inquiries to be unseemly and at times rude. Some of these conversations degenerated into heated arguments. Tr. at 768. However, none of these witnesses testified that Respondent Huntsinger ever told them that they must order tests from joint venture laboratories as a condition for remaining limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer.

The I.G. did not prove that Respondents directed Respondent Huntsinger to hector partners into ordering more tests or to oust those who were not ordering enough tests. The evidence as to instructions Respondent Huntsinger may have had from Respondent Hanlester or its principals concerning either making calls or the substance of those calls essentially is that Respondent Tasha asked Respondent Huntsinger to ascertain from limited partners whose referrals had decreased what problems they were experiencing with the quality and timeliness of the laboratories' service. Findings 124 - 126. Respondent Huntsinger testified that he did have authority to offer unhappy partners the return of their investments. Tr. at 2348.

The I.G. did not prove that Respondent Huntsinger systematically called those limited partners who ordered relatively few tests. Further, there is little probative evidence as to the substance of Respondent Huntsinger's communications to Respondents about his telephone conversations, apart from Respondent Huntsinger's recollections that some physicians expressed unhappiness about the operations of the laboratories. Tr. at 2348 - 2355. Such evidence would have been significant, inasmuch as Respondent Huntsinger was not a principal in or employed by Respondent Hanlester. There is no evidence to show what, if any, authority he had to make decisions concerning partnership status on behalf of Respondent Hanlester, beyond having the authority to offer unhappy partners the refund of their investments.

Respondent Huntsinger had reasons to call limited partners other than to assert discipline, and his motives may have been misinterpreted by some of these partners. Respondent Huntsinger may also have misinterpreted the communications he received from some limited partners. Respondent Huntsinger was retained by SKBL as medical director of Respondents PPCL and Omni. Finding 114. Respondent Huntsinger contacted limited partners in his capacity as medical director to attempt to resolve problems that they were having with the joint venture laboratories' services. These calls were placed at a time when there were significant problems with laboratory services. Findings 121 - 123. Given the context of these calls, it is not unreasonable to infer that at least some limited partners would have given Respondent Huntsinger a piece of their minds concerning the problems they were experiencing. Given their annoyance with the manner in which the laboratories were operating, these physicians could easily have read more into Respondent Huntsinger's communications than what he intended. It is reasonable to conclude that Respondent Huntsinger interpreted these physicians' anger as a request to have their investments returned to them.

The most logical explanation for Respondents' refunding partnership investments to Drs. Rubin, Luster, and Saraf is that Respondents and these physicians misunderstood each other. It is evident from these physicians' testimony of their conversations with Dr. Huntsinger that the tone of these conversations was unpleasant. Dr. Rubin testified that he told Dr. Huntsinger to "go f___ himself." Tr. at 768. Dr. Huntsinger easily might have interpreted this expletive as a demand to be excused from the partnership. It is unclear that Drs. Rubin, Luster, and Saraf wanted to remain limited partners after this telephone conversation with Dr. Huntsinger. None of these physicians asked or demanded that Respondents reinstate them after he received the refund of his investment.

Other evidence offered by the I.G. about Respondents' communications with limited partners and their motives for making such communications is neither persuasive, in and of itself, nor in combination with other evidence, including the evidence relating to Respondent Huntsinger's telephone calls. One SKBL employee testified that, based on a conversation he had with Respondent Tasha, he inferred that partners who failed to order business from joint venture laboratories would be ousted from the partnerships. Tr. at 543 - 544. Another witness, Dr. ReVille (a limited partner), testified Respondent Tasha told him "something on . . . (the) order" that ways would be found to have "non-heavy" producers in joint venture laboratories use their money more effectively. Tr. at 1439. A third witness, Paul Rust, an SKBL employee, testified that it was his understanding from conversations he had with Respondent Tasha and others that limited partners would be ousted from the joint ventures for failure to make use of the joint ventures' laboratories. Tr. at 507. The I.G. also adduced testimony that Respondent Tasha had stated that he expected limited partners to make use of joint venture laboratories. Tr. at 783.

I am not persuaded by this testimony for several reasons. First, the fact that a Respondent may have expected limited partners to patronize joint venture laboratories does not, by itself, permit an inference to be drawn that Respondents conditioned ownership of limited partnership shares on partners' agreements to patronize the laboratories. Nor does it suggest that Respondents intended to discipline those partners who did not order tests from the laboratories. An underlying premise of the joint ventures was that partners would use the laboratories. But that would be so whether Respondents envisioned partners voluntarily using the laboratories or being compelled to do so.

Second, the witnesses' recollections of what Respondent Tasha may have said were not precise and were in critical respects contradicted by other evidence. For example, Dr. ReVille contradicted his own testimony by testifying that he purchased limited partnership shares as an investment and did not consider himself obligated to patronize joint venture laboratories. Tr. at 1442.

Finally, Respondents credibly denied that they had conditioned ownership of partnership shares on purchasers' agreements to refer business. Their testimony was consistent with what was contained in Respondent Hanlester's offering statements and Mr. Aprahamian's testimony.

The I.G. offered the testimony of SKBL employees that Respondents had ousted some limited partners who had not ordered sufficient business. This testimony is less than compelling. None of these witnesses had any direct knowledge of Respondents' actions. For the most part, their testimony was based on assumptions formed from conversations with other individuals. For example, Mr. Rust prepared an internal presentation for other SKBL employees which asserted that Respondent Hanlester had "booted out" eight limited partners. See I.G. Ex. 39.0; Tr. at 429 - 432. This witness' conclusion in his presentation was based on conversations that he may have had with another SKBL employee or Respondent Tasha, and not on direct knowledge. Tr. at 502 - 503, 505, 510. Mr. Rust could not precisely recall what he had been told concerning partners' ouster or who communicated the information to him. Both the SKBL employee from whom the witness thought he obtained the information that limited partners had been ousted and Respondent Tasha denied ever communicating such information. Tr. at 2126, 2217.

Another SKBL employee testified that she had been told by Ms. Hitchcock that a limited partner could be "cancelled" by Respondent Hanlester for insufficient use of a joint venture laboratory. Tr. at 806. However, that same employee testified that Respondent Tasha had told her that Respondent Hanlester could not "cancel" a limited partner. Tr. at 836 - 837.

The I.G. also offered the testimony of a physician, Dr. Bond, who had been a limited partner in Respondent PPCL. Dr. Bond testified that, at a meeting of limited partners, an individual whom he thought might have been Respondent Lewand stated that Respondent Hanlester would repurchase the shares of partners who could not utilize joint venture laboratories. Tr. at 1641. Dr. Bond could not recall the precise statement which this individual made. Respondent Lewand, on the other hand, denied saying that non-contributing partners would be bought out. He testified that he had told the participants at that meeting that the basis for Respondent Hanlester repurchasing a partner's shares would be that partner's death, retirement, closing his practice, or if 51 percent of the partners agreed that it would be detrimental to the partnership's interest for the limited partner to remain. Finding 135.

Although it is evident that many people attended this meeting, and several may have heard Respondent Lewand's statement, the I.G. did not produce any witness to that statement besides Dr. Bond.[7] I do not conclude that

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[7] On cross-examination, Respondent Huntsinger testified that he was present when Respondent Lewand made the statement. His recollection was that Respondent Lewand:

> (S)tated clearly that the partnership, per se, could not do anything against a partner that didn't want to produce any work, that we were -- our hands were tied.

Tr. at 2361 - 2362.

Respondent Lewand told the participants at the meeting that Respondent Hanlester would buy back the shares of a partner who failed to contribute business to a joint venture laboratory. I base my conclusion on his forceful denial, Dr. Bond's less-than-complete recall of the statement, and the I.G.'s failure to produce testimony which would more clearly recount what Respondent Lewand said.

The I.G. also offered evidence to show that Respondent Hanlester maintained charts and other records to monitor the number of tests ordered by limited partners in the joint ventures. Finding 119. The I.G. argues that I should infer that the purpose of such monitoring was to track partners' utilization in order to discipline those partners who did not order sufficient business from joint venture laboratories. I do not draw that inference, because there exists a more plausible and benign explanation for this practice.

As I note above, the joint venture laboratories depended on the business generated by limited partners. These partners were the laboratories' preferred customers. A significant decline in any limited partner's utilization of a joint venture laboratory would serve as a warning signal to the laboratory that there was a problem with the service provided to that partner, and possibly, with service in general. Given that, it would be a normal and rational business practice for the laboratories to monitor partners' utilization rates. I do not attach significance to the fact that the joint ventures were not devoting similar efforts to monitor non-partners' business. These accounts comprised only a small percentage of the joint ventures' business, and a decline in utilization by a non-partner would not necessarily signal the existence of a meaningful problem. Respondents would not have obtained the intelligence about their operations from monitoring non-partners' accounts that they obtained from monitoring partners' accounts.

Perhaps the most compelling reason for concluding that the I.G. did not prove that Respondents disciplined limited partners who failed or refused to order tests is the I.G.'s failure to offer any meaningful evidence, aside from the testimony of Drs. Rubin, Luster, and Saraf, that Respondents actually ousted anyone.[8] More

[8] The I.G. also introduced the affidavit of a fourth physician, Dr. Martin, and an interview report of Dr. Martin which was prepared by an I.G. special agent.

than one hundred physicians became limited partners in Respondent PPCL, Respondent Omni, or Respondent Placer. Respondent PPCL was in operation for nearly three years prior to the commencement of these cases. Respondents Omni and Placer were in operation for nearly two years. A number of limited partners ended their investments in these Respondents. However, the I.G. failed to introduce evidence as to specifically which partners had left the partnerships, or the reasons for their doing so. The I.G. did not offer any evidence to correlate those partners who did leave the partnerships with the amount of business they had ordered, or to compare their laboratory utilization with that of partners remained.

In contrast, there is evidence which shows that Respondents tolerated limited partners who did not order substantial tests from joint venture laboratories. Some limited partners ordered few tests and remained partners in good standing. Finding 139. There was little correlation between limited partners' ownership interests and the number or value of the tests that they ordered. See I.G. Ex. 14.0, 65.0, 68.0; Ha Ex. 57.

I am not persuaded that Respondents paid limited partners an unusually high rate of return on their investments in order to induce them to refer business to joint venture laboratories. The I.G. failed to prove that Respondents' distribution to limited partners was atypically high when compared to distributions to limited partners from other health care joint ventures. Finding 200; Tr. at 208 - 209. Moreover, no partner's return was directly related to the amount of tests that that partner ordered from a joint venture laboratory. Finding 196. Respondents PPCL, Omni, and Placer made distributions to each limited partner based on net profits and on that partner's equitable ownership interest. Finding 195. Each partner's equitable ownership interest was based on the number of shares the partner owned. A partner

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I.G. Ex. 104.0. I attach little weight to these documents. Dr. Martin was not called to testify by the I.G. In his affidavit, Dr. Martin says that Respondent Huntsinger implied that he would be "dropped" from Respondent PPCL because of his failure to order sufficient tests. However, Dr. Martin does not provide his recollection of what Respondent Huntsinger said, as opposed to the implications of what Respondent Huntsinger said.

could order no tests, or the partner could order many tests, without directly affecting his or her partnership distribution.

E. <u>The relationship between Respondents Hanlester, PPCL, Omni, Placer, and SKBL</u>

The I.G. makes two assertions concerning the management relationship between Respondents Hanlester, PPCL, Omni, Placer, and SKBL. First, the I.G. contends that, as a consequence of this management relationship, the joint venture laboratories were "fraudulent" operations which performed no meaningful functions. The I.G. argues that Respondents assumed no operating risks or meaningful costs under the management agreements. Respondents PPCL, Omni, and Placer, merely functioned as conduits for monies to be paid to physicians to induce them to refer business, according to the I.G. Second, the I.G. argues that the management agreements concealed "indirect" remuneration from SKBL to Respondents in return for the referral of tests from Respondents PPCL, Omni, and Placer, to SKBL.

The management relationship between Respondents Hanlester, PPCL, Omni, Placer and SKBL provided advantages to all parties. The principal advantage to Respondents was that it enabled them to shed most of the day-to-day operating responsibilities for the joint ventures' laboratories, albeit for a substantial price. The principal advantage to SKBL was that, in return for undertaking to manage the laboratories, SKBL received substantial compensation based on a stream of referrals. However, neither Respondents or SKBL operated pursuant to a hidden agenda. I am not persuaded that, on close scrutiny, evidence as to the management relationship between Respondents and SKBL contributes significantly to the I.G.'s claim that Respondents paid remuneration to limited partners to induce them to refer business. The I.G. did not prove that Respondents received remuneration from SKBL in return for referring business. To the contrary, the evidence shows that Respondents remunerated SKBL for its management services.

The management relationship was memorialized in a master laboratory services agreement between Respondent Hanlester and SKBL, and in laboratory management agreements between Respondents Hanlester, PPCL, Omni, and Placer, and SKBL. Findings 143, 146, 160, 162. In the master laboratory services agreement, SKBL promised to provide laboratory management services to all joint venture laboratories in which Respondent Hanlester had an ownership interest. Finding 145.

The laboratory management agreements specified the terms on which SKBL would manage laboratories owned by Respondents PPCL, Omni, and Placer. Respondents PPCL, Omni and Placer were required to provide facilities and equipment necessary for the operation of clinical laboratories. Finding 147. These Respondents were required to repair and maintain laboratory space and to pay utility charges. SKBL was obligated to provide and compensate all staff necessary to operate the joint venture laboratories, to supervise the laboratories' administrative and operational activities, and to conduct all billing and collection activities on the laboratories' behalf. Findings 149 - 153. SKBL was to be compensated for its management of each joint venture's laboratory with a monthly management fee from each joint venture of 76 percent of net cash receipts. Findings 154, 155.

The effect of this relationship was to relieve Respondents Hanlester, PPCL, Omni, and Placer of the day-to-day responsibilities for operating joint venture laboratories. SKBL had the contractual duty to staff and operate the joint venture laboratories. To the extent that problems in administering these laboratories arose, SKBL had the obligation to resolve them.

SKBL opted to refer most of the tests ordered from Respondents PPCL, Omni, and Placer to its own central processing facilities in Van Nuys and Dublin, California. Findings 181 - 183. SKBL could have elected to perform all tests at facilities operated by Respondents PPCL, Omni, and Placer. The I.G. argues that SKBL's decision to refer most of the PPCL, Omni, and Placer laboratory tests to central processing facilities proves that these Respondents' laboratories were sham operations whose principal function was to serve as a conduit of monies to remunerate physicians for referring tests.

The I.G. further asserts that the management arrangement with SKBL facilitated Respondents' payments to obtain referrals, because it eliminated all meaningful risk and costs to Respondents. According to the I.G., the true nature of the relationship between SKBL and Respondents becomes apparent on close examination of the structure and operations of the joint ventures' laboratories. This assertion devolves into a contention that the laboratories were "shells" which performed no meaningful function. According to the I.G., they were used by Respondents and SKBL to conceal a relationship wherein laboratory tests ordered by limited partners were purchased en masse from Respondents by SKBL. The I.G. asserts, in effect, that the revenues from these tests were "laundered" by Respondents to make it look as if they were revenues received from tests which Respondents performed.

I disagree with the I.G.'s contentions. There is no evidence which shows that the relationship between SKBL and Respondents was intended to conceal payments or to "launder" payments from SKBL through Respondents to physicians in return for referrals. The decisions which Respondents and SKBL made concerning the management of Respondents PPCL, Omni, and Placer reflect relatively common practices in the health care industry which have legitimate business objectives unrelated to payment for referred business.

The management relationship between Respondents and SKBL does not, on its face, suggest fraudulent intent. The fact that Respondents PPCL, Omni, and Placer contracted with SKBL to have SKBL manage their operations reflects a relatively common practice in the clinical laboratory field. It is not unusual for a company like SKBL to agree to manage a laboratory. Tr. at 185, 191. It is not unusual for an independent clinical laboratory, like Respondents PPCL, Omni, and Placer, to refer business to a larger laboratory. Finding 185.

SKBL's decision to centrally process the joint ventures' laboratory tests can be explained by rational economic considerations having nothing to do with the issue of payments to limited partners. Efficiency considerations drove SKBL's decision to refer tests to its central facilities. Findings 184 - 186. It was in SKBL's pecuniary interest to process tests as efficiently as possible. Its profits depended on the extent to which its administrative and operating costs for the joint ventures' laboratories fell below 76 percent of the laboratories' revenues. Finding 166. SKBL decided that it could more economically process tests centrally than it could process them at the joint venture laboratories. SKBL could have exercised the same discretion under the management agreements irrespective of the structure and ownership of Respondents PPCL, Omni, and Placer. For example, the identical efficiency considerations would have pertained under the management agreements had these Respondents been single-owner proprietorships.

It is not true that the management agreements eliminated all meaningful costs to Respondents Hanlester, PPCL, Omni, and Placer. Under these agreements, Respondents assumed substantial costs. A small but not insignificant percentage of the tests ordered from Respondents PPCL, Omni, and Placer were performed at these joint ventures' laboratories. Findings 188 - 190. Respondents were required to purchase and maintain sufficient equipment so that the joint venture laboratories were equipped to perform those tests. Finding 147. The joint ventures were also required to furnish and maintain laboratory space and to pay utility charges. Finding 149.

The greatest cost assumed by Respondents was the cost of compensating SKBL for its services. The compensation which Respondents paid to SKBL for its services comprised substantial costs which were rationally related to the expenditures necessary to operate the joint ventures. It simply begs the question of whether these payments were a meaningful cost to Respondents to argue that the management agreements saved them the costs of staffing and operating laboratories.

Nor is it true that the management agreements eliminated Respondents' business risk. Respondents placed the responsibility for running the joint ventures in the hands of SKBL. That decision was to Respondents' advantage only insofar as SKBL operated the laboratories in a manner which satisfied the laboratories' customers, who essentially were limited partners. Finding 167. Failure by SKBL to satisfy these limited partners by providing timely and efficient service would jeopardize these partners' loyalty to the joint ventures' laboratories and could, in turn, cause Respondents to experience a loss in business and revenues.

In fact, there is evidence that SKBL's management of the laboratories was, at least for a time, less than optimal. Respondents PPCL, Omni, and Placer experienced problems both with the timeliness of their tests and with billing for services. Findings 121 - 123; Ha Ex. 40; Tr. at 1478, 1487. At least one partner in Respondent Omni sold back his partnership share to Respondent Hanlester because of billing problems. Tr. at 1794 - 1795.

Perhaps the greatest risk assumed by Respondents in entrusting management of Respondents PPCL, Omni, and Placer to SKBL is that the relationship would fail altogether. See Tr. at 212 - 213. The management agreements provided either party with the option to terminate the agreement upon 90 days' notice. See I.G. Ex. 4.1/8. A decision by SKBL to pull out of the relationship with Respondents would likely cause collapse of the limited partnerships. Respondents emphasized the SKBL relationship as a selling point in marketing limited partnership shares. The relationship was a critical element in persuading physicians to become limited partners. As the I.G.'s expert, Thomas L. Kelly, testified:

> It is my opinion that the SmithKline arrangement was a substantial contributor to the marketability of the limited partnership units and it may well have been unmarketable without the SmithKline arrangement.

Tr. at 136.

The I.G. argues that the agreements with SKBL concealed an "indirect" remuneration from SKBL to Respondents to pay for referrals of laboratory tests from limited partners. According to the I.G., the value of the payments given to Respondents from SKBL greatly exceeded the fair market value of the services provided by the joint venture laboratories. Therefore, according to the I.G., an inference can be drawn that SKBL was remunerating Respondents for the referrals of laboratory tests ordered by limited partners.

This argument is fatally flawed, because it fundamentally mischaracterizes the relationship between Respondents Hanlester, PPCL, Omni, Placer, and SKBL. SKBL did not purchase tests from Respondents, nor did it compensate Respondents for services provided by joint venture laboratories. To the contrary, Respondents compensated SKBL for the services it provided. As I find supra, this compensation was substantial, consisting of 76 percent of monthly revenues from each joint venture. I find nothing in the management agreements or in the parties' face-to-face relationships to suggest that Respondents received any remuneration from SKBL for referred business.

The I.G. asserts that unlawful payments can be discerned in the manner in which SKBL distributed revenues to Respondents PPCL, Omni, and Placer. The I.G. contends that these distributions manifest an intent by SKBL to pay Respondents for referrals. The I.G. also argues that the distributions enabled

Respondents in turn to pay limited partners for referrals.

Pursuant to the management agreements, SKBL deposited the receipts earned by Respondents PPCL, Omni, and Placer into separate accounts which SKBL maintained for each of these Respondents. Findings 168, 169. SKBL made revenue distributions to Respondents PPCL, Omni, and Placer, from these accounts. Finding 170. In October, 1987, SKBL decided to make distributions to Respondent PPCL based on expected revenue (based on tests performed and billed for) rather than on actual receipts. Subsequently, SKBL distributed revenues to Respondents Omni and Placer based on the same formula. Findings 171, 176. SKBL continued to make distributions to the joint ventures based on this formula throughout the life of its management agreements with these Respondents.

The I.G. contends that payments made on this "accrual" basis overstated the distributions that Respondents and, ultimately, limited partners were entitled to receive. The I.G. argues that such distributions were, in effect, payments from SKBL to Respondents in return for referrals. He asserts that Respondents were able to induce referrals from physicians by redistributing the "extra" compensation they received from SKBL in the form of partnership returns.

This analysis is not supported by the evidence. It is true that the "accrual" distributions made by SKBL to Respondents PPCL, Omni, and Placer initially were greater than what would have been distributed based on actual revenues. Finding 172. Such distributions certainly enabled Respondents to make greater initial partnership distributions than had distributions from SKBL been based on actual collections. Finding 179. However, the "accrual" distribution system did not require SKBL to make greater total distributions to Respondents PPCL, Omni, and Placer than it had otherwise agreed to make pursuant to the management agreements. Finding 178. Nor did it permit Respondents to make greater total distributions to their limited partners than would otherwise have been possible. Finding 180.

SKBL treated the difference between what it distributed based on the "accrual" system and what it had actually collected in laboratory revenues as an advance against future distributions. Finding 173. SKBL intended eventually to recoup from Respondents that which it had advanced. Id. Although the "accrual" distributions from SKBL to Respondents can be characterized as a loan against future revenues, they cannot be characterized as a payment for referrals.[9]

III. The meaning of section 1128B(b)(2) of the Act

Much of the I.G.'s case against Respondents hinges on his contentions concerning the interpretation of section 1128B(b)(2). If, as the I.G. contends, section 1128B(b)(2) proscribes an offer or payment to induce a party to refer program-related business, without regard to whether the offer is conditioned on the offeree's promise to refer program-related business, then the I.G. need not prove that the offers to sell limited partnership interests in this case were conditioned on physicians agreeing to refer business to the joint venture laboratories.

If the I.G.'s interpretation of section 1128B(b)(2) is correct, then Respondents violated the Act by offering payments to physicians in the form of returns on the physicians' limited partnership investments and by urging those physicians to refer business to the joint venture laboratories. Respondents concede that they advised prospective purchasers of limited partnership interests that it would be in their pecuniary interest to refer business to the joint venture laboratories. The sales materials furnished by Respondents to potential participants told them that not referring tests to the laboratories would be a "blueprint for failure" of the joint ventures. I.G. Ex. 2.0/6.

The I.G.'s interpretation would not only direct a finding that Respondents violated the Act, but it would also seem to imperil an array of transactions in the health care field which involve program-related business. The I.G.'s interpretation would threaten any joint venture among health care providers whose structure and compensation formulas encouraged participants to refer business to the joint ventures

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[9] Although distributions were made on the "accrual" system throughout the life of the management agreements, there was no evidence offered by the parties as to whether the total of these distributions exceeded the total collections of laboratory revenues for services ordered from the joint ventures. Nor was evidence offered to show whether, at some point, SKBL and any of Respondents engaged in an effort to balance what had been distributed against what had actually been collected.

even if such joint ventures do not require referrals as a quid quo pro for participation.

I conclude that, in enacting section 1128B(b)(2), Congress prohibited agreements by health care providers which precluded them from making choices which were in the financial or quality of care interest of federally-funded health care programs and their beneficiaries and recipients. These prohibited agreements included bribes, kickbacks, and rebates, and similar arrangements. The unifying characteristic of the conduct which Congress proscribed is that it consists of offers of agreements or agreements which foreclose the options of health care providers to order services which are cost-efficient and which are of the best quality. Offers or payments that were intended to influence provider choice, as opposed to agreements which foreclosed provider choice, are not within the scope of the legislative prohibition.[10]

An essential element of a violation under section 1128B(b)(2) is the offer of an agreement or an agreement to refer program-related business. The section does not proscribe offers or payments which may be calculated to encourage offerees to refer business but which do not require referrals as a condition for payment.

A. The evolution and history of section 1128B(b)

The evolution and history of the Act demonstrates that, in enacting section 1128B(b), Congress was concerned with offers and agreements to pay kickbacks as a quid pro quo for referred business. There is nothing which suggests that Congress intended the Act to proscribe arrangements which encouraged parties to make referrals as opposed to unethical agreements which required such referrals.

The original version of the Act, adopted in 1972, made it unlawful for a party to solicit, offer, or receive any kickback or bribe in connection with the furnishing of a program related item or service. It also made it unlawful for a party to solicit, offer, or receive a rebate of any fee or charge for referring a program beneficiary to another person for the furnishing of an

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[10] I am not suggesting by this distinction that Congress always regards as benign actions that influence provider choice. As I shall discuss, infra, Congress has opted to prohibit such actions in some circumstances.

item or service. Pub. L. No. 92-603, 242(b), 86 Stat. 1329, 1419 (1972).[11]

The legislative history to the 1972 Act shows that Congress was concerned with prohibiting unethical or anticompetitive agreements:

> Your committee believes that a specific provision defining acts subject to penalty under the Medicare and Medicaid programs should be included to provide penalties for certain practices which have long been regarded by professional organizations as unethical, as well as unlawful in some jurisdictions, and which contribute appreciably to the cost of the Medicare and Medicaid programs. Thus, under the committee bill, the criminal penalty provision would include such practices as the soliciting, offering, or accepting of kickbacks or bribes, including the rebating of a portion of a fee or charge for a patient referral, involving providers of health care services.

H.R. Rep. No. 92-231, 92nd Cong., 1st Sess. 107-108 (1971), reprinted in 1971 U.S. Cong. Code & Admin. News 4989, 5093 (emphasis added).

The current language of section 1128B(b), originally adopted in 1977, broadened the scope of prohibited conduct by defining it to consist of the knowing and willful payment of "any remuneration (including any kickback, bribe, or rebate) directly or indirectly, overtly or covertly, in cash or in kind." Social Security Act, section 1128B(b)(1), (2). Under the current language, prohibited remuneration includes, but is not limited to, bribes, kickbacks, and rebates. Congress intended the Act to proscribe all forms of this traditionally unethical conduct. However, neither the revisions nor the legislative history suggest that Congress ever intended the Act to proscribe forms of conduct which were beyond the ambit of that which was traditionally viewed as anticompetitive or unethical, including kickbacks, bribes, or rebates. In particular, neither the revisions nor legislative history suggest that Congress intended to proscribe

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[11] The section which applied to the Medicare program was contained in section 1877(b) of the Act. Identical language which applied to Medicaid was contained in section 1909(b).

conduct which encouraged providers to refer program-related business.

Congress felt it necessary to revise the Act because the Act did not effectively reach the unethical or anticompetitive conduct that it had intended to prohibit. H.R. Rep. No. 95-393 (II), 95th Cong., 1st Sess. 53 (1977) reprinted in U.S. Cong. Code & Admin. News 3039, 3055. Congressional committees expressed concern that fraudulent or unethical agreements were being disguised in a way which concealed their purpose. H.R. Rep. No. 95-393, supra. For example, the Senate Special Committee on Aging, in a 1977 committee report, found that kickbacks remained a problem despite enactment of the 1972 Act. The Committee found overwhelming evidence that:

> (M)any pharmacists are required to pay kickbacks to nursing home operators as a precondition of obtaining a nursing home's business. Pharmacists also must pay rebates to practitioners or other owners of medicaid mills, the small 'shared health care facilities' which checker the ghettos of our major cities.

Kickbacks Among Medicaid Providers, S. Rep. No. 320, 95th Cong., 1st Sess. (1977), at 28. (emphasis added). The committee also found that:

> It is evident that kickbacks are frequently required from clinical laboratories if they hope to obtain the business of both medicaid mills and nursing homes. Committee investigators are convinced that laboratories are barred from obtaining a medicaid account unless they pay kickbacks.

Id. (emphasis added).

The committee's report extensively detailed circumstances where pharmacies were coerced by nursing homes into paying kickbacks as a condition for receiving the homes' business. It also detailed circumstances where laboratories covertly offered payments to physicians to obtain the physicians' agreements to refer Medicaid business.

In an earlier report, the committee found that kickbacks by clinical laboratories to physicians to obtain Medicaid business continued despite the 1972 Act. Fraud and Abuse Among Clinical Laboratories, S.

Rep. No. 94-944, 94th Cong., 2d Sess. (1976). The Committee surveyed practices in several states and concluded that the payment of kickbacks by laboratories in order to obtain physicians' business was an uncontrolled problem.

> It appears to the subcommittee -- based upon firsthand investigation and analyses of findings from other States -- that kickbacks are so rampant that laboratories are almost barred from obtaining a Medicaid account unless they offer a kickback.

Id. at 47 (emphasis added).

My conclusion that Congress did not intend section 1128B(b) to prohibit conduct which encourages providers to refer program-related business is reinforced by its recent enactment of legislation which prohibits some forms of business that encourage referrals. Congress would have had no need to enact such legislation if section 1128B(b) already prohibited such arrangements. In 1989, Congress enacted section 6204 of the Omnibus Budget Reconciliation Act of 1989. This section, which became section 1877 of the Act, and which becomes effective in 1992, prohibits a physician who has either an ownership interest in or a compensation arrangement with an entity such as a laboratory, from making any referrals of Medicare business to that entity. It appears that this section will, when effectuated in 1992, bar physicians from making Medicare-reimbursable referrals to clinical laboratories in which they have an ownership interest. The new law is aimed at arrangements which encourage providers to make referrals.

B. Statutory language and construction

The language of the Act and the manner in which the courts have applied it demonstrate that Congress prohibited agreements to refer program-related business. The Act cannot reasonably be interpreted to prohibit offers or payments which are intended to encourage referrals but which are not conditioned on referrals of program-related business.

In interpreting and applying section 1128B(b), I must apply the same rules of construction as would be applied by a federal court in a criminal enforcement proceeding. Section 1128B(b) is a criminal statute and therefore must be construed narrowly. This case arises by virtue of the fact that in 1987 Congress expanded section 1128 of the Act to include exclusion of individuals and entities who were found to have violated section 1128B(b). Social Security Act, section 1128(b)(7). Congress provided that, in such cases, the petitioner would ordinarily be entitled to a hearing before an administrative law judge before the exclusion could be effectuated. Social Security Act, section 1128(f)(2). Congress did not provide that section 1128B(b) should be interpreted or applied more broadly in civil proceedings under sections 1128(b)(7) and (f)(2) than in criminal enforcement proceedings in federal courts.

It is an accepted maxim of statutory interpretation that criminal statutes should ordinarily be construed narrowly. United States v. Emmons, 410 U.S. 396, 411 (1973). That rule governs my interpretation of the Act, because I am applying a criminal statute in a civil remedies proceeding. Application of the rule does not mean that I should interpret the Act so narrowly as to frustrate the intent of Congress. On the other hand, I should not overreach to extend the boundaries of the Act into areas which are beyond what Congress intended to prohibit.

I am particularly concerned that I not apply the Act in a manner which exceeds the reach established by federal courts in criminal cases because to do so would risk creating an "administrative" interpretation of the Act which is not accepted beyond the corridors of the Department. There is nothing in the letter of the Act or in its history to suggest that Congress intended that there exist divergent criminal and administrative interpretations.

Congress did not define the term "any remuneration" in its 1977 revision. Absent a statutory definition, this term ought to be assigned its common and ordinary meaning. Webster's Third New International Dictionary (1969) defines "remuneration" to include the act or fact of remunerating. It defines "remunerate" as:

> 1: to pay an equivalent for (as a service, loss, expense) 2: to pay an equivalent to (a person) for a service, loss, or expense . . . .

The common and ordinary meaning of "remuneration" therefore is a payment in return for a service, loss, or expense. As used within section 1128B(b), the term means payment in return for a quid pro quo.[12]

In its 1977 revision Congress qualified the term "any remuneration" with the words "kickback," "bribe," and "rebate." The juxtaposition of these terms in the Act means that Congress intended that the term "any remuneration" not only include kickbacks, bribes or rebates, but that proscribed remuneration be of a character similar to kickbacks, bribes, or rebates.

An established tenet of statutory construction is that words in statutes should be construed in light of the words with which they are associated. Schrieber v. Burlington Northern, Inc., 472 U.S. 1, 8 (1985); Auto-Ordinance Corp. v. United States, 822 F.2d 1566, 1571 (Fed. Cir. 1987). Similarly, general terms in statutes should be read to mean things which are similar to those things which are specifically enumerated as illustrative of the general terms. Central Forwarding, Inc. v. Interstate Commerce Commission, 698 F.2d 1266, 1279 (5th Cir. 1983); Trinity Services, Inc. v. Marshall, 593 F.2d 1250, 1258 (D.C. Cir. 1978); See Harrison v. PPG Industries, Inc., 446 U.S. 578, 588, (1980). Application of these principles to the language of section 1128B(b) reinforces the conclusion that "any remuneration" means traditionally unethical agreements, such as agreements to pay bribes, kickbacks, or rebates.

I find that Congress' use of the words "kickback," "bribe," and "rebate" to qualify the term "any remuneration" is further evidence that Congress intended to proscribe agreements to refer business. As shall be discussed infra, in every case where the courts have found such unlawful remuneration, the underlying misconduct consists of offers of agreements or agreements to refer program-related business.

Courts use words like "kickback" and "bribe" to mean offers or agreements to make payments in exchange for something given in return. For example, in United

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[12] One commentator has concluded that the term "any remuneration" in section 1128B meant payment in return for a service, loss, or expense. Yoakum, Physician Fraud in the Medicare-Medicaid Programs -- Kickbacks, Bribes and Remunerations, 10 Memphis State University L. Rev. 684, 693 (1980).

States v. Hancock, 604 F.2d 999 (7th Cir. 1979), the court stated that "kickback" is:

> commonly used and understood to include "a percentage payment . . . for granting assistance by one in a position to open up or control a source of income," Webster's Third New International Dictionary (1966), and we think it was used in the statute to include such a payment.

604 F.2d at 1002. The unlawful scheme in Hancock consisted of payments to physicians in return for sending medical specimens to laboratories. The term "bribery" has been defined to mean the voluntary giving of anything of value in corrupt payment for an official act done or to be done. United States v. Zacher, 586 F. 2d 912, 914 (2d Cir. 1981). Thus, the terms used by Congress to describe prohibited payments, including "remuneration," "kickback," "bribe," and "rebate" have commonly been defined to mean agreements to pay something in exchange for something of value.

The purpose of section 1128B(b)(2) to prohibit agreements to refer program-related business becomes more apparent when that section is read in context with the other parts of section 1128B(b). Section 1128B(b)(2) is aimed at the offerors and payors of remuneration to induce referrals. The other side of the equation is addressed by section 1128B(b)(1), which prohibits parties from knowingly and willfully soliciting or receiving any remuneration, including any kickback, bribe, or rebate "in return for" referring program-related business (emphasis added). Congress' intent to prohibit offers and payments of remuneration for agreements to refer business in section 1128B(b)(2) is evident when sections 1128B(b)(1) and 1128(B)(b)(2) are read in pari materia, because section 1128B(b)(1) plainly prohibits agreements. Given the law's history and the meaning of its language, there would be no point in giving asymmetrical application to the two sections.[13]

Furthermore, the only subsection of section 1128B(b) which is even arguably ambiguous as to what Congress intended to prohibit is subsection 1128B(b)(2)(A),

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[13] In United States v. Bay State Ambulance and Hospital Rental Service Inc., 874 F.2d 20 (1st Cir. 1989), the court stated as dicta that "(C)ongress meant the crimes to have the same elements for payor and payee." 874 F.2d at 34.

which prohibits payments of remuneration to induce a person:

> to refer an individual to a person for the furnishing or arranging for the furnishing of any item or service for which payment may be made . . . .

This subsection, when read in isolation, could be construed to support the I.G.'s "inducement equals encouragement" theory of unlawfulness. However, subsection 1128B(b)(2)(B), which is also aimed at the offeror or payer of remuneration, prohibits payments of remuneration to induce a person:

> to purchase, lease, order, or arrange for or recommend purchasing, leasing, or ordering any good, facility, service, or item for which payment may be made . . . .

As with section 1128B(b)(1), the plain meaning of this language is that payments to induce agreements to refer business are unlawful. Therefore, the I.G.'s statutory construction argument reduces to relying on the wording of one arguably ambiguous subsection of the Act. Any possible ambiguity in that subsection is eliminated when it is read in context, as it should be.

C. Judicial application of the Act

The courts have not held that proof of an agreement to refer program-related business is a prerequisite to establishing a violation of section 1128B(b)(2). However, the cases in which courts have found violations of section 1128B(b)(2) or its predecessor involve offers of agreements or agreements to refer program-related business. In each of these cases, the defendants were found to have purchased referrals through some remuneration scheme or to have offered to purchase referrals. None of the cases have found unlawful an offer or payment which is intended to encourage referrals, but which does not require referrals as a quid pro quo for acceptance of the offer or payment.

Commonly, the unlawful offer contains a formula pursuant to which payments will be made based on the value of the business which the offeree agrees to refer. The courts often, but not always, refer to such remuneration as a kickback. For example, in United States v. Duz-Mor Diagnostic Laboratory, Inc., 650 F.2d 223 (9th Cir. 1981), the defendants were convicted of unlawfully offering to pay remuneration as an inducement for the referral of medical services that were reimbursable from Medicare and Medi-Cal (the California Medicaid program) funds. The defendants' unlawful scheme was found to consist of offering providers a 15 percent rebate in exchange for the referral of Medicare and Medi-Cal business. 650 F.2d at 227. In United States v. Universal Trade and Industries, Inc., 695 F.2d 1151 (9th Cir. 1983), the defendants were convicted of unlawfully offering remuneration to induce a provider to purchase the defendants' laboratory services. The unlawful scheme consisted of a disguised kickback to a physician for referrals of laboratory tests to defendants. Defendants offered to establish a laboratory in the physician's clinic and to kick back a fixed percentage of the gross revenues of the laboratory to the physician. 695 F.2d at 1152-1153.[14]

In United States v. Greber, 760 F.2d 68 (3rd Cir. 1985), the defendant was convicted for, among other things, unlawfully paying remuneration to physicians to induce them to refer Medicare business. The scheme consisted of kicking back a percentage of each fee that defendant received from Medicare for providing cardiac monitoring services to the physician who referred the monitoring request to defendant. Although the court did not focus on the elements of the agreement between the defendant and individual physicians, it is apparent that the quid pro quo for each kickback was a referral. 760 F.2d at 71.

In United States v. Lipkis, 770 F.2d 1447 (9th Cir. 1985), the unlawful remuneration consisted of kickback payments of approximately 20 percent of the revenue from referred laboratory tests. In United States v. Kats, 871 F.2d 105 (9th Cir. 1989), the unlawful

[14] The I.G. relies on the Universal Trade decision as addressing the broad scope of the statutory term "remuneration." See I.G.'s Brief at 18. He characterizes the offense found by the court as being grounded on a laboratory's "making net profit distributions to the owner of a clinic that made referrals to the lab." Id. What was at issue in Universal Trade was an agreement to pay kickbacks for referrals. The parties explored various mechanisms to disguise that unlawful agreement. In the final analysis, the violation of the Act was premised on the agreement, not on the artifices which the parties used to disguise it. 695 F.2d at 1152 - 1153.

remuneration consisted of an agreement to kick back 50 percent of the Medicare payments received by a laboratory as a consequence of referrals from a provider. 871 F.2d at 106-107.

Variants of this type of agreement have also been the basis for convictions for unlawfully offering or paying remuneration. Although the payment schemes may vary, the common thread of the cases is that the unlawful schemes are premised on the provider's agreement to refer program-related business to the payor. For example, in United States v. Stewart Clinical Laboratory, Inc., 635 F.2d 804 (9th Cir. 1981), the scheme consisted of offering a physician free laboratory tests for the physician's private patients, if that physician agreed to refer his Medi-Cal business to the defendant laboratory. 652 F.2d at 805.[15]

D. The I.G.'s misplaced reliance on the term "to induce"

Much of the I.G.'s argument as to the meaning of section 1128B(b)(2) focuses on the statutory phrase "to induce."
The I.G. argues that the phrase "to induce" is synonymous with the phrase "to encourage." Based on this analysis, the I.G. contends that a party offering to make payments may violate the Act if his or her intent was to influence another to make referrals even though the other party has not agreed to make referrals. I.G.'s Brief at 21. The I.G. argues that unlawful intent may be discerned by examining the payment a party offers to another to encourage that party to refer program-related business. According to the I.G., if the payment is high in relation to the value of that which is performed by the party who receives the payment and refers business, then that party has been unlawfully "induced" to refer business within the meaning of section 1128B(b)(2).

I disagree with the I.G.'s analysis. It does not comport with what Congress intended to prohibit. It relies on a literal application of the phrase "to induce" without due regard to the context in which it is used, legislative history, the maxims of statutory construction, and judicial decisions which have applied the Act to specific facts. It incorrectly presumes that the Act sought to prevent any payments which influenced or encouraged a provider to refer business,

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[15] This case was reversed on other grounds.

when in fact the Act was directed at agreements to refer business.

The I.G. asserts that his analysis is supported by several recent judicial decisions. These include Lipkis, Greber, Kats, and United States v. Bay State Ambulance and Hospital Rental Service, 874 F.2d 20 (1st Cir. 1989). The I.G. relies on the courts' statements in these cases that the gravamen of fraud under section 1128B(b)(2) is the inducement factor.

I conclude from my reading of Lipkis, Greber, Kats, and Bay State, that there are circumstances where a trier of fact may infer the existence of an agreement to refer program-related business from the nature and circumstances of a payment. A party who makes payments in return for referrals of program-related business is very likely going to disguise these payments in order to evade the scrutiny of law enforcement officials, including the I.G. These decisions make it plain that a trier of fact may pierce through a disguise in order to identify an unlawful payment. The contention that a payment is ostensibly for a legitimate purpose is not a defense if that payment is also made as remuneration for referrals. And if the value of a payment substantially exceeds the fair market value of that which the payment ostensibly purchased, then a trier of fact may reasonably infer that the balance of the payment has been made as remuneration for referrals.[16] However, none of these decisions support the contention that section 1128B(b)(2) proscribes payments which are made in a context which encourages a party to refer program-related business, but which are not conditioned on the payee agreeing to refer program-related business.

In Lipkis, the court found that the fair market value of that which was given back to the payor by the recipient of payments was substantially less than the value of the payments. The court found from this evidence that there was no question that the payments

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[16] That does not mean, however, that "excessive" compensation proves a violation of the Act or that a violation may be presumed from "excessive" compensation. A reasonable inference may be drawn from payment which exceeds the value of that which ostensibly has been purchased that something unstated has been purchased as well. However, there may be benign explanations for the payment, which could negate the inference.

were being made for referrals as well as for other services. 770 F.2d at 1449.

However, in Lipkis, the parties had entered into an agreement to refer business in exchange for kickbacks. 770 F.2d 1449. The evidence cited by the court is evidence from which the unlawful agreement was inferred. There is nothing in the Lipkis decision to suggest that the court intended its holding to stand for the proposition that section 1128B(b)(2) proscribed payments intended to encourage referrals.

Close analysis of the Greber decision does not support the I.G.'s contention that section 1128B(b)(2) prohibits parties from making payments to encourage referrals. As I note above, the facts of Greber suggest a scheme to make payments in return for referrals. There is no finding in the decision that the payments were being made merely to encourage referrals. The court's statement in Greber "that the statute is aimed at the inducement factor," 760 F.2d at 71, does not address the question of whether an agreement is necessary to violate section 1128B(b)(2). Rather, it addresses the question of whether an unlawful agreement can be inferred from the circumstances of a payment. The defendant in Greber contended that if some legitimate purpose existed for the compensation he paid to physicians (payment for services rendered) then no violation could be established. He argued that a violation could only be shown if the sole purpose of payments was to induce referrals. The court disagreed with this contention, finding that a party could violate the Act if one purpose of its payments to another was to induce referrals. 760 F.2d at 72.

The Kats decision is very similar to Greber. The conduct on which the conviction in Kats was based consisted of an agreement to kick back Medicare payments. 871 F.2d 105-106. As in Greber, the defendant argued that his payments could not be construed as evidence of a violation unless their sole purpose was to induce the making of referrals. The court disagreed, citing the Greber decision as authority for its conclusion that a party could violate the Act if only one purpose of his or her making payments to another was to induce referrals. 871 F.2d at 108.

As with Lipkis, Kats, and Greber, Bay State does not support an argument that a party may violate the Act simply by offering or paying a sum to another to encourage that person to refer program-related business. Bay State supports the proposition that a party may violate the Act if that party offers or makes a payment to another to induce the referral of program-related business, regardless whether the value of the payment exceeds the value of what is given by the payee. In one sense, it states a broader rule of evidence interpretation than is contained in the I.G.'s assertion that a violation may be inferred if the payment exceeds that which is obtained in return. However, the main point of Bay State is that bribes paid to corruptly influence the referral of program-related business will be a basis for finding a violation of the Act, even if they are disguised to look like legitimate payments for services.

The defendant in Bay State was a corporation which provided ambulance service. The defendant had bid for, and been awarded, a contract to provide emergency ambulance service to a municipal government. The defendant had covertly hired as a consultant the municipal employee who bore principal responsibility for drafting specifications for the ambulance service contract, for evaluating bids, and for recommending a bid award. This employee had recommended that the contract be awarded to the defendant. The defendant was charged with, and convicted of, unlawfully paying remuneration for the referral of program-related business. The defendant argued on appeal that the trial court erred in its instruction to the jury. According to the defendant, the trial court should have instructed the jury that it could not convict unless it found that the payments made by the defendant were not reasonable payments for the actual services provided by the municipal employee as part of his consultant relationship.

The United States Court of Appeals for the First Circuit rejected this argument. It held that a payment made as an inducement to refer business may evidence a violation of the Act, regardless whether the value of the payment exceeded the value of that which was performed by the recipient. 874 U.S. at 29. In reaching its decision, the court did not specifically address the issue of whether the municipal employee agreed to influence the bid award as consideration for his covert consultant arrangement with the defendant. The facts of the case imply such agreement. The question of whether a payment made to encourage referrals violates the Act simply was not an issue in the case.

E. <u>The Secretary's authority to adopt "safe harbor" regulations</u>

Congress amended the Act in 1987 to authorize the Secretary, in consultation with the Attorney General, to adopt regulations specifying payment practices that shall not be treated as criminal violations of section 1128B(b) and which shall not serve as a basis for exclusion under section 1128(b)(7). Social Security Act, section 1128B(b)(3)(D); Pub. L. 100-93, section 14(b)(3). Although "safe harbor" regulations have been published for comment, they have not been finally adopted. I draw no conclusions as to how the Act should be interpreted from the proposed regulations.

Even when finally adopted, the "safe harbor" regulations would not serve as a basis for determining what is prohibited by the Act. The Secretary's authority to declare exceptions to the Act is not authority to declare conduct to be illegal.

Congress gave the Secretary a limited <u>quasi-legislative</u> authority to decide whether certain payment practices would be permitted regardless whether they might violate the Act. Pursuant to section 1128B(b)(3)(D), the Secretary might decide that a payment practice should be protected because it satisfies a public policy objective, irrespective of whether it would otherwise fall within the statutory prohibition. That determination could be made by the Secretary without deciding the question of whether the payment practice is illegal. The fact that the Secretary does not opt to except a payment practice does not mean that the practice violates the Act. It means that the Secretary has not chosen, pursuant to his <u>quasi-legislative</u> authority, to carve out a special protection for that payment practice.

F. <u>The implications of the I.G.'s interpretation</u>

There are additional compelling reasons for concluding that the I.G.'s interpretation of section 1128B(b)(2) is incorrect. The I.G.'s interpretation would, if followed to its logical end, proscribe payment practices which do not appear to be unethical or anticompetitive and which are commonplace in the health care market. <u>See</u> Ha Ex. 33. Furthermore, the I.G.'s interpretation would, if accepted, result in a law which does not define in reasonably neutral terms that which is illegal. These consequences of the I.G.'s interpretation of the Act are results which Congress did not intend:

> All laws should receive a sensible construction. General terms should be so limited in their application as not to lead to injustice, oppression or an absurd consequence. It will always, therefore, be presumed that the legislature intended exceptions to its language which would avoid results of this character.

United States v. Kirby, 74 U.S. 482, 486-487 (1868).

The inexorable consequence of the I.G.'s logic is that any offer to a health care provider which involves payments which are in any way intended to encourage that provider to refer program-related business would violate the Act. A limited partnership joint venture whose partners' compensation might be indirectly affected by business they refer to the joint venture's facilities would appear to be per se illegal.[17] An agreement among physicians to jointly own and operate a clinical laboratory would be suspect, because implicit in such arrangement is the fact that each participant's compensation would at least indirectly be affected by the amount of business he referred to the laboratory. An offer by a hospital to a physician to join a medical staff which includes any payment, in cash or in kind, would be suspect because it could be viewed as an inducement to the physician to refer patients to the

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[17] For example, under the I.G.'s interpretation, any offer to a physician to invest in a joint venture laboratory would violate section 1128B(b)(2) if the offeror told the physician that his or her investment return from the laboratory would be affected by the referrals the physician made to the laboratory. I am skeptical that this relationship between investment return and referrals is not routinely communicated to potential physician partners in joint venture clinical laboratories. An obvious reason for such laboratories is that their participants stand to profit from referrals. Joint venture clinical laboratories enable physicians to profit from the Medicare-reimbursed laboratory tests that they order. The Act prohibits physicians from claiming reimbursement from Medicare for tests performed by independent laboratories. Social Security Act, section 1833(h)(5)(A).

hospital. See Ha Ex.36.[18] A promotional gift of medications to a physician by a drug company's sales representative would be suspect, because it could be viewed as an inducement to the physician to recommend to his patients that they purchase the drug company's medications. None of these practices involve agreements to refer business as a condition of the payment, yet all would be potentially illegal under the I.G.'s interpretation, because they contain "inducements" to make referrals.

Congress never suggested that it intended to prohibit any of the aforesaid practices by its enactment of section 1128B(b). The Act was directed at agreements which traditionally have been viewed as unethical or anticompetitive. There may be public policy reasons to condemn payments which encourage providers to refer program-related business. However, such payments were not the target of section 1128B(b).

The I.G. denies that the Act is as sweeping in its prohibitions as his interpretation implies. At the hearing, the I.G.'s counsel stated that the Act did not, for example, proscribe per se all provider-owned health care joint ventures. See Tr. at 1877.[19] However, the I.G. has never offered any logical basis

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[18] Indeed, the act of taking a prospective hospital medical staff member to lunch could be interpreted to be an unlawful inducement.

[19] However, the I.G. asserts in his Reply Brief that:

> The term 'any remuneration' is not limited to payments that are similar to bribes, kickbacks, and rebates. It is a broad term, meaning the transfer of anything of value in any form or manner whatsoever. The term 'to induce' does not require that the recipient has agreed to make any referrals to the payor. It means that the payor attempts or seeks to influence or persuade the recipient to make referrals.

I.G.'s Reply Brief at 99. The I.G. has not shown how this formula would not render per se illegal virtually all health care joint ventures, as well as most promotional activities directed towards providers of health care items or services by those who seek to attract their business.

to distinguish that which his interpretation impliedly proscribes from that which he wants to proscribe.

The I.G. contends that the Act provides two ways to distinguish prohibited from permissible conduct. First, health care providers may look to future "safe harbor" regulations as guidelines. Second, a payment will not be suspect if what is paid for is not excessive in relation to the value of what is received in return for the payment. These criteria do not provide a meaningful basis for distinguishing lawful from unlawful payments.

As I note above, the "safe harbor" regulations have not been adopted. No party can or should be expected to condition his conduct on the basis of proposals which have not been implemented. If adopted, these regulations will not determine which conduct is lawful, apart from the conduct which is specifically excepted from the reach of the Act by the Secretary. Therefore, they will not provide a mechanism to predict whether conduct will violate the Act.

I find no statutory basis for the I.G.'s second criterion. This formula is not a principled basis to separate lawful from unlawful conduct so much as it is an artifice to save the I.G. from having to confront the inevitable consequence of his logic. As I note above, it depends on a misplaced reliance on the statutory term "to induce." Congress did not say that the lawfulness of payments to providers depends on measuring those payments against the value of items or services provided. Moreover, the I.G.'s second criterion contradicts his own interpretation of the Act. If payments which encourage a party to refer business are unlawful, it should not matter whether the payments are excessive in relation to other, legitimate, services provided. See my discussion of Bay State, supra. Any payment made to encourage the referral of program-related business, no matter how small or ineffectual, should violate the Act under the I.G.'s analysis.

In any event, the formula advocated by the I.G. is an imprecise and vague test which fails to provide anyone with a reasonable basis for determining whether his or her conduct would contravene the Act. The I.G. never states how much compensation would be too much compensation under his formula. Under the I.G.'s interpretation, a party would be forced to continuously measure the payments he made to another against what he received in return to assure that the ratio of payments to returns is not too high. An inefficient entrepreneur who offered low returns on investment to participants in a joint venture might escape prosecution, whereas a successful entrepreneur who earned large profits and paid high returns would be susceptible to prosecution as a result of his efficiency. Few would risk the prospect of exclusion from participation (if not criminal prosecution and conviction) in such an environment.[20] I suspect that most simply would opt not to engage in any business transaction which <u>might</u> be construed to be illegal.

The I.G. asserts that any interpretation of section 1128B(b)(2) which is narrower than his "inducement equals encouragement" formula would improperly constrict his discretion to prosecute violators of the Act. His underlying contention is that Congress intended the Act to have very broad implications, but left it to the I.G. to decide as a policy matter how the law is to be applied. The I.G. argues that I am improperly usurping his policy making role if I construe the Act more narrowly than he would have it be construed.

The I.G. mischaracterizes my role in interpreting and applying the Act. I am not charged with making policy. In adjudicating this case, I must resolve the parties' contentions as to the meaning of the Act, and my decision may indirectly have some policy implications. I am not engaging in policy making by construing the law more narrowly than the I.G. wants and by identifying the correct interpretation of the Act nor am I interfering with the legitimate functions of the I.G. The construction which I have given to section 1128B(b)(2) is certainly narrower than that which the I.G. advocates. It is consistent with Congressional intent and the letter of the Act, as well as with the judicial injunction that criminal statutes not be construed broadly.

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[20] As I note <u>supra</u>, an inference of an unlawful agreement may be drawn in some cases from the circumstances of a payment. But that does not mean that a case can be decided simply by comparing the payment with that which is received in return for the payment.

IV. What must be proven to establish a violation under sections 1128B(b)(1) and 1128B(b)(2)

As I note above, sections 1128B(b)(1) and 1128B(b)(2) of the Act address the two sides of an equation. Section 1128B(b)(1) defines those circumstances where the recipient of a payment may be found to have violated the Act. Section 1128B(b)(2) defines those circumstances where a party who offers or makes a payment may be found to violate the law.

A. Intent

To violate section 1128B(b)(1), a party must knowingly and willfully solicit or receive a prohibited payment. To violate section 1128B(b)(2), a party must knowingly and willfully offer or make a prohibited payment. The term "knowingly and willfully" identifies the intent which must necessarily be established in order to prove a violation. The test for intent was established in the Kats and Greber decisions as being the intent to do something prohibited by the Act. It is not necessary under this test to establish that a party had a specific intent to violate the Act, nor is it necessary to establish that the sole or even the primary purpose of the party charged with the violation was to engage in prohibited conduct. It will suffice to show that one purpose of a party was to engage in conduct prohibited by the Act. Greber, 760 F.2d at 69. Even if actions also have a legitimate purpose other than that which is prohibited, the requisite intent will be established if one purpose of the actions is to accomplish something that is prohibited. Id. at 72.

Thus, a party will manifest the requisite intent to violate section 1128B(b)(1) if that party agreed to accept payments in return for referring program-related business, even if that party also accepted the payments for other, lawful, reasons. A party will manifest the requisite intent to violate section 1128B(b)(2) if that party offered to make payments, or actually made payments, for a prohibited purpose, even if that party also made the payments for other, legitimate reasons.[21]

[21] A more detailed explication of the intent standard is contained in my May 8, 1990 Ruling.

B. Agreement to refer program-related business

To violate section 1128B(b)(1), a party must knowingly and willfully solicit or receive remuneration in return for referring a program-related item or service. As is discussed above, the meaning of this section is plain. Whatever payment is solicited or received by the referring party must be intentionally solicited or received by that party as a condition for that party agreeing to refer program-related business.

To violate section 1128B(b)(2), a party must knowingly offer or pay any remuneration conditioned on the recipient of the payment agreeing to refer program-related business. It will not suffice to establish a violation to show that payments were offered or made in the hope that a provider would be encouraged to refer program-related business.

V. Analysis of Respondents' conduct in the context of section 1128B(b)

The I.G. did not prove that any of Respondents unlawfully received remuneration from SKBL in return for referring program-related business, in violation of section 1128B(b)(1) of the Act. The I.G. did not prove that Respondents Lewand, Tasha, Welsh, Huntsinger, Keorle, PPCL, Omni, or Placer offered or paid remuneration for referrals of program-related business in violation of section 1128B(b)(2) of the Act. The I.G. proved that Respondents Hanlester, PPCL, Omni, and Placer, by virtue of the acts of their agent Ms. Hitchcock, offered remuneration for referrals of program-related business in violation of section 1128B(b)(2) of the Act.

A. Analysis of Respondents' conduct pursuant to section 1128B(b)(1)

In order for me to find that any of Respondents violated section 1128B(b)(1), I must conclude that that Respondent knowingly and willfully solicited or accepted remuneration from SKBL in return for referring program-related business. *See* Part IV A of this Analysis. The I.G. did not prove that any Respondent solicited or received remuneration from SKBL. Therefore, the I.G. did not establish that any Respondent committed a violation of section 1128B(b)(1).

The I.G. argues that Respondents received "indirect" remuneration from SKBL in return for referring program-related business to SKBL. As I find above, SKBL made no payments to Respondents. To the contrary, Respondents PPCL, Omni, and Placer made substantial payments to SKBL to remunerate SKBL for its management services.

That is not to say that Respondents did not benefit from their management relationship with SKBL. The management agreements provided Respondents with substantial advantages, which I have enumerated in detail in Part II. The I.G. intends his term "indirect remuneration" to encompass such benefits. But the Act does not attach liability to parties simply because they benefit from contracts. In order for there to be a violation under section 1128B(b)(1), there must be proof that the charged party solicited or received some payment, in cash or in kind, in return for agreeing to refer program-related business. The I.G. failed to prove that Respondents solicited or accepted payments from SKBL.

Nor did the I.G. prove that Respondents agreed to refer program-related business to SKBL. The management agreements do not guarantee SKBL a flow of business from Respondents PPCL, Omni, and Placer.

B. Analysis of Respondents' conduct pursuant to section 1128B(b)(2)

In order for me to find that any of Respondents violated section 1128B(b)(2), I must conclude that the Respondent knowingly and willfully offered or gave remuneration to that party to induce that party to refer program-related business. Implicit in this section is the requirement that the offer or the payment be conditioned on the recipient's agreement to refer program-related business. Unconditional offers or payments do not violate section 1128B(b)(2). See Parts III and IV B of this Analysis.

There is ample evidence that Respondents intended to encourage limited partners to refer business to the joint ventures. One of Respondents' central objectives was to capture and profit from the referrals made by limited partner physicians. As I hold, supra, Respondents drew an explicit link between referrals and profits. They made it obvious to limited partners that the limited partnership laboratories gave limited partners the opportunity to profit indirectly from that which they could not profit directly. They made it equally obvious that the limited partnerships would fail if limited partners did not refer business to the partnerships' laboratories.

However, the I.G. did not prove that any of Respondents intended that the sale of limited partnerships in Respondents PPCL, Omni, and Placer be conditioned on the limited partners agreeing to refer program-related business to joint venture laboratories. Respondents did not intend that the sale of shares or the payment of dividends to individual limited partners be conditioned on the amount of program-related business that individual limited partners either agreed to refer or actually referred to to joint venture laboratories. Respondents did not intend to discipline partners who failed to refer sufficient business, either by ousting them from the partnerships or by threatening to oust them.

Nor is there evidence that Respondents paid dividends to individual limited partners based on the volume of their referrals. To the contrary, the evidence establishes that what a limited partner received depended entirely on his ownership share as a percentage of those joint venture profits which were set aside for distribution to limited partners. Finally, the I.G. did not prove that Respondents actually disciplined partners by ousting those who failed to refer sufficient business to joint venture laboratories.

There is a clear distinction, however, between what Respondents intended and what Ms. Hitchcock said on their behalf. Ms. Hitchcock implied to prospective limited partners that their eligibility to purchase shares in Respondents PPCL, Omni, and Placer depended on their agreement to refer program-related business. She told them explicitly that the number of shares that they would be permitted to purchase would depend on the amount of business they were able and willing to refer. She told them that partners who did not refer business would be pressured to leave the partnerships.

These representations by Ms. Hitchcock were made in the course of a sales pitch in which she promised prospective limited partners large profits and little or no investment risk. When considered in context, Ms. Hitchcock's representations constitute knowing and willful offers of remuneration to induce physicians to refer program-related business.

1. Liability of Respondents Hanlester, PPCL, Omni, and Placer for the acts of their agent Ms. Hitchcock

There was an explicit agency relationship between Ms. Hitchcock and Respondent Hanlester. Ms. Hitchcock also was the agent of Respondents PPCL, Omni, and Placer. She represented herself to be the agent of both Hanlester and the limited partnership Respondents. Finding 92. Nothing contained in Respondents' sales material suggested otherwise.

The Act applies to entities as well as to individuals. Section 1128B(b) broadly applies to "whoever" commits a proscribed offense. The term "whoever" is sweeping enough to apply to any form of business organization, including partnerships. It is apparent from the Act's legislative history that Congress was concerned not just with individuals who offered, paid, or received proscribed remuneration, but with entities as well. See Part III A of this Analysis. Courts have applied the Act to entities, including corporations. See, e.g., United States v. Universal Trade and Industries, Inc., 695 F.2d 1151 (9th Cir. 1983).

The Secretary's authority to impose a civil remedy against a party who violates section 1128B(b) derives from section 1128(b)(7), which applies to "any individual or entity" whom the Secretary determines has committed an act described in section 1128B. Section 1128(b)(7) therefore engrafts onto section 1128B its own definition of who may be subject to a civil remedy for violation of section 1128B. Congress sought to apply section 1128(b) broadly, as is apparent from its use of the term "any individual or entity" to define those who fell within the scope of the section. I conclude that the reach of section 1128(b) extends to include partnerships, as well as individuals and corporations.

Under section 1128B(b), an entity such as a partnership may be liable for the acts of its agents. It is a settled principle of federal law that a partnership may be held criminally liable for the acts of its agents. United States v. A & P Trucking Company, 358 U.S. 121 (1958). In A & P Trucking, the United States Supreme Court found that a partnership could be found criminally liable for the acts of its agent, based on the doctrine of respondeat superior. 358 U.S. at 125. In that case, the Court addressed the policy which underlies the need to hold entities, including partnerships, responsible for the acts of their agents:

> The business entity cannot be left free to break the law merely because its owners . . . do not personally participate in the transaction. The treasury of the business may not with impunity obtain the fruits of violations which are committed knowingly by agents of the entity in the scope of their employment. Thus pressure is brought on those who own the entity to see to it that their agents abide by the law.

358 U.S. at 126.

Identical considerations apply here. In these cases, Respondents Hanlester, PPCL, Omni, and Placer permitted their agent Ms. Hitchcock to engage in conduct which was within the scope of her agency relationship and which violated section 1128B(b)(2). In engaging in such conduct, Ms. Hitchcock committed Respondents Hanlester, PPCL, Omni, and Placer to a course of action even though such action was not authorized by these Respondents' principals. I conclude that these Respondents are liable for her acts based on the principles of respondeat superior.

2. Liability of Respondents Lewand, Tasha, Welsh, Huntsinger, and Keorle for the acts of Ms. Hitchcock

The I.G. argues that, pursuant to the law of agency, derivative liability may attach from a partnership to an individual partner. Therefore, according to the I.G., Respondents Lewand, Tasha, Welsh, Huntsinger, and Keorle must be held accountable for the unlawful conduct of Respondents Hanlester, PPCL, Omni, and Placer, even if there is no proof that Respondents Lewand, Tasha, Welsh, Huntsinger, and Keorle personally engaged in or authorized proscribed conduct.

I disagree with the I.G.'s contention. A party may not be found to have violated section 1128B(b) without a showing of necessary intent. Liability does not attach to a party under section 1128B(b) simply because that party is a principal in an entity which has been found to have violated the Act.

A party cannot be found to have violated section 1128B(b) absent proof that that party knowingly and willfully engaged in proscribed conduct. It is not sufficient evidence to hold a party accountable to show that an entity in which a party has some ownership interest engaged in proscribed conduct. More must be proved. At a minimum, it must be shown that the party charged with the violation approved of or directed the proscribed conduct.[22]

The fact that a party has an interest in an entity which engages in criminal conduct is not a sufficient basis to find that party liable for the criminal conduct. Nor may a shareholder or a partner in an entity be found criminally liable based only on actions of the entity's agent, absent proof that the shareholder or partner authorized or approved the agent's actions. That is not to say that the acts of an agent are irrelevant to the ultimate issue of liability. The agent may execute an unlawful plan. The agent's acts may therefore prove a plan's implementation. However, the relationship between an agent of an entity and a partner in that entity is on its face too remote to conclusively presume that the agent's acts were authorized or approved by the partner.

This analysis is in accord with principles of federal criminal law which require that scienter must ordinarily be established as a prerequisite to a finding of guilt. In the A & P Trucking Company case, the Supreme Court observed that a partner could not personally be held liable for the criminal acts of a partnership absent proof that the partner was personally responsible for those acts. 358 U.S. at 127. Thus, an entity may be held criminally liable based on the criminal acts of an agent acting within the scope of his or her agency, whereas the agent's acts are not, in and of themselves, sufficient grounds to hold a principal of the entity criminally liable. Id.

The I.G. has cited a number of decisions to support his argument that partners in Respondent Hanlester should be held liable under section 1128B(b)(2) based on a

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[22] For example, had the I.G. proven that any of Respondents directed or authorized Ms. Hitchcock to make unlawful representations to prospective limited partners, then the I.G. would have established that that Respondent had violated the Act. Liability would be premised on that Respondent's conduct and intent, and not on his status as a principal in Respondents Hanlester, PPCL, Omni, or Placer.

finding that Respondent Hanlester violated the Act. The cases cited by the I.G. are civil cases. While they may support the proposition that in civil actions, a partner may be liable for the wrongful acts of his partnership, they do not establish that the same principle applies under federal criminal law. See, e.g., Danzig v. Jack Grynberg & Associates, 161 Cal. App. 3d 1128, 208 Cal. Rptr. 336 (1984).

It is true that this is a civil remedies proceeding, not a criminal case. However, in order to establish that authority exists to exclude a party under section 1128(b)(7), the I.G. must prove that the party "committed an act which is described" in section 1128B. Social Security Act, section 1128(b)(7). The import of this language is that the I.G. must prove that a party has committed an act which would violate section 1128B, in order to establish authority to impose a remedy under section 1128(b)(7). The standard for liability under section 1128B is criminal, not civil. The I.G. fails to meet the criminal liability standard of section 1128B by proving only that a party has engaged in conduct which might meet a civil liability standard.

Here, the evidence does not show that Respondents Tasha, Welsh, or Keorle, acting as principals in Respondent Hanlester, approved or directed the acts of Respondents Hanlester, PPCL, Omni, and Placer which violated section 1128B(b)(2). The unlawful acts were caused by an agent who acted contrary to their direction. Therefore, these Respondents are not personally liable for the unlawful conduct of Respondents Hanlester, PPCL, Omni, and Placer which resulted from the Ms. Hitchcock's acts.

Several of Respondents against whom the I.G. seeks to attach derivative liability were not in fact principals in Respondent Hanlester. None of them were principals in Respondents PPCL, Omni, or Placer.[23] Respondent Lewand had no direct interest in Respondent Hanlester. Respondent Huntsinger owned no interest in Respondent Hanlester. Neither Respondents Lewand, Tasha, Welsh, Huntsinger, or Keorle were principals in Respondents PPCL, Omni, or Placer. Thus, even if the I.G.'s theory of liability were correct, liability would not attach to Respondents Lewand and Huntsinger as principals in Respondent Hanlester, or against Respondents Lewand,

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[23] Respondent Lewand was an owner of Hanlester Corporation, which, at one time, was a principal in Respondent Hanlester.

Tasha, Welsh, Huntsinger, or Keorle as principals in Respondents PPCL, Omni, or Placer.[24]

Finally, I conclude that Respondent Huntsinger cannot be held liable as an agent of Respondents PPCL, Omni, and Placer for the conduct of his co-agent, Ms. Hitchcock. I am unaware of any authority which would hold an employee or an agent criminally liable for the conduct of a co-worker, absent proof that the employee or agent personally participated in the unlawful conduct.

3. Liability of Respondents Lewand, Tasha, Welsh, Huntsinger, and Keorle for their statements and acts

The I.G. did not prove that Respondents Lewand, Tasha, Welsh, Huntsinger, or Keorle knowingly and willfully offered or paid remuneration to limited partners in Respondents PPCL, Omni, or Placer to induce them to refer program-related business, in violation of section 1128B(b)(2). Therefore, based on their statements and conduct, these Respondents are not liable for violating section 1128B(b)(2).

I have considered the question of these Respondents' liability under section 1128B(b)(2), both in light of evidence concerning their statements and conduct and evidence as to the nature of the offers and payments they made or directed be made to limited partners in Respondents PPCL, Omni, and Placer. The I.G. did not prove that these Respondents' statements establish unlawful intent or acts. See my discussion of each of these Respondents' statements at subparts a. through e., infra. Nor can unlawful intent or acts be concluded from the dividends paid to limited partners in Respondents PPCL, Omni, or Placer.

As I note at part III D of this Analysis, there are circumstances where an unlawful agreement to refer program-related business may be inferred from the

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[24] Furthermore, Respondent Welsh ceased being a principal in Respondent Hanlester in the Summer of 1987. Finding 12. Hanlester Corporation, the predecessor to Respondent Keorle, was a principal in Respondent Hanlester. However, it sold its interest in January 1989. There is no theory of liability which would make either Respondents Welsh or Keorle liable for acts occurring after they ceased to be principals in Respondent Hanlester.

nature of the payments which are offered or made to health care providers. Greber, 760 F.2d at 72. A bribe may be disguised as a legitimate consulting fee, as was the case in Bay State, 874 F.2d at 29. Kickbacks or rebates may be disguised as rent for facilities, consulting fees, or dividends. Payments which bear no legitimate relationship to that which is received in return are suspect.

The payments which Respondents offered and made to limited partners in Respondents PPCL, Omni, and Placer do not prove unlawful agreements to refer business. Certainly, Respondents structured the terms of participation in Respondents PPCL, Omni, and Placer to make it highly attractive for physicians to participate. It is obvious, as I have observed supra, that Respondents needed these physicians to refer tests to the joint ventures' laboratories in order for the laboratories to succeed. However, the manner in which Respondents compensated limited partners does not suggest that there was a hidden condition of participation consisting of a requirement that these partners refer business. Payments were made to limited partners whether or not those partners referred business to the laboratories. Payments were made based on the partners' equitable ownership shares and were not based on the amount of business that partners referred. Payments were made based on the laboratories' revenues. Thus, the payments made to individual limited partners in Respondents PPCL, Omni, and Placer do not establish a nexus between the referrals made by the individual partners and the compensation each of them received. Absent such nexus, I cannot infer an unlawful agreement to remunerate partners for referrals.

The I.G. did not prove that the structure of Respondents PPCL, Omni, and Placer demonstrated a fraudulent intent. The business decisions made by Respondents are explained by legitimate business and efficiency considerations. The joint venture laboratories, in their structure and operation, resembled joint ventures commonly established in the health care market. As the I.G.'s own expert, Mr. Kelly, admitted, these joint ventures were a "generic type of limited partnership." Tr. at 181. The returns that the limited partnerships offered and paid to partners were not unusually high. Tr. at 209.

a. Respondent Lewand

The I.G. did not prove that Respondent Lewand told physicians that they would be permitted to purchase joint venture shares if they agreed to order tests from joint venture laboratories. Nor did he prove that Respondent Lewand conditioned the number of shares that were sold to any physician on the amount of business that physician agreed to refer. The I.G. did not prove that Respondent Lewand threatened to oust those partners who did not refer business, nor did the I.G. prove that Respondent Lewand authorized the ouster of partners who did not refer business. See Part II D of this Analysis.

The only evidence the I.G. offered concerning statements that Respondent Lewand may have made linking ownership of joint venture shares to an agreement to refer business to a joint venture is the testimony of Dr. Bond, which I discuss at Part II D of this Analysis. For the reasons which I have expressed, I am not persuaded that this evidence establishes that Respondent Lewand engaged in conduct which violated the Act.

b. Respondent Tasha

The evidence offered by the I.G. concerning Respondent Tasha is similarly unpersuasive. As is described in Part II D, there was conflicting and equivocal testimony from some witnesses that Respondent Tasha said that partners who did not refer business to joint venture laboratories would be ousted from the partnerships. That evidence was weakened by its imprecision and was outweighed by Respondent Tasha's credible denial that he made such statements. I conclude that the I.G. did not prove that Respondent Tasha conditioned ownership of shares in Respondents PPCL, Omni, and Placer on physicians agreeing to refer business. Nor did the I.G. prove that Respondent Tasha authorized the ouster of partners because those partners had failed to refer sufficient business to joint venture laboratories.

c. Respondent Welsh

There is no credible evidence to prove that this Respondent engaged in acts prohibited by section 1128B(b). Respondent Welsh was involved with Respondent Hanlester and the marketing of limited partnership shares in Respondent PPCL only until the Summer of 1987. He actively participated in the formation of Respondent PPCL and the marketing of this joint venture's shares. There is no credible evidence that he ever told prospective partners that they must agree to refer business as a condition for purchasing shares, or that he conditioned the number of limited partnership shares which were offered to any prospective limited partner on the amount of business that that physician agreed to refer to a joint venture laboratory. There is no evidence to link Respondent Welsh to the administration of Respondent Hanlester or Respondent PPCL.

d. Respondent Keorle

The I.G. did not prove that Respondent Keorle violated section 1128B(b)(2). Respondent Keorle is the successor in interest to Hanlester Corporation. Hanlester Corporation was a majority owner of Respondent Hanlester prior to January 1989 and was in part owned by Respondent Lewand.

The I.G. offered no evidence to show precisely what role Hanlester Corporation played in the management of Respondent Hanlester. It is reasonable to infer that the management decisions of this corporation were the same as management judgments made by Respondent Lewand. The I.G. offered nothing to prove that Hanlester Corporation ever conditioned ownership of shares in Respondents PPCL, Omni, or Placer on purchasers agreeing to refer program-related business. Nor did the I.G. prove that Hanlester Corporation conditioned the number of shares a limited partner could buy on the amount of business that partner agreed to refer to a joint venture laboratory. The I.G. offered no evidence to show that Hanlester Corporation ever threatened to oust, or actually ousted, limited partners who failed to refer business to joint venture laboratories.

e. Respondent Huntsinger

The I.G. did not prove that Respondent Huntsinger told prospective limited partners in Respondents PPCL, Omni, or Placer that they would be permitted to purchase shares if they agreed to refer program-related business to joint venture laboratories. The I.G. did not prove that Respondent Huntsinger conditioned the number of shares that a prospective partner could purchase on the amount of business that that prospective partner was willing to refer.

The I.G. offered substantial testimony to show that, in his capacity as medical director of Respondents PPCL and Omni, Respondent Huntsinger called limited partners and asked them why they were not ordering more tests from joint venture laboratories. Respondent Huntsinger's tone and the substance of these inquiries was plainly considered to be obnoxious by some of the limited partners. At least a few of these telephone conversations degenerated into confrontations.

However, the evidence does not establish that Respondent Huntsinger threatened limited partners with removal for failure to refer business, nor does it establish that Respondent Huntsinger or other Respondents ousted these partners because they had failed to refer business. See Analysis at Part II D. Respondent Huntsinger's communications with limited partners, no matter how obnoxious or irritating these partners may have considered them to be, did not violate section 1128B(b)(2).

VI. Remedy

The I.G. requested that I impose and direct exclusions against Respondents from participating in Medicare and Medicaid. The length of the proposed exclusions varies from three years for Respondent Welsh to permanent exclusions for Respondents PPCL, Omni, and Placer. I do not have authority to impose and direct exclusions against those Respondents whom I have found did not violate section 1128B(b) (Respondents Lewand, Tasha, Welsh, Keorle, and Huntsinger). No remedial purpose would be served by imposing and directing exclusions against those Respondents whom I have found to have violated section 1128B(b)(2) (Respondents Hanlester, PPCL, Omni, and Placer). Therefore, I decline to impose and direct exclusions against any Respondent.

The I.G. brought these cases pursuant to section 1128 of the Act. Section 1128(b)(7) gives the Secretary the authority to exclude individuals or entities whom he has determined have violated sections 1128A or 1128B. No exclusion may be imposed pursuant to section 1128(b)(7) unless a finding has been made that the respondent has violated either section 1128A or 1128B.

I have found that four of the Respondents, Respondents Hanlester, PPCL, Omni, and Placer, violated section 1128B(b)(2). Authority exists to exclude each of these Respondents. The question which remains is whether an exclusion of any of these Respondents is needed to satisfy the remedial purposes of section 1128.

Section 1128 is a civil remedies statute. The remedial purpose of section 1128 is to enable the Secretary to protect federally-funded health care programs and their beneficiaries and recipients from individuals and entities who have proven by their misconduct that they are untrustworthy. Exclusions are intended to protect against future misconduct by providers. See Berney R. Keszler M.D. et al., DAB Civ. Rem. C-167 at 32 (1990).

Federally-funded health care programs are no more obligated to continue to deal with dishonest or untrustworthy providers than any purchaser of goods or services would be obligated to deal with a dishonest or untrustworthy supplier. The exclusion remedy allows the Secretary to suspend his contractual relationship with those providers of items or services who are dishonest or untrustworthy. The remedy therefore enables the Secretary to assure that federally-funded health care programs will not continue to be harmed by dishonest or untrustworthy providers of items or services. See Keszler at 32 - 33. The exclusion remedy is therefore closely analogous to the civil remedy of termination or suspension of a contract to forestall future damages from a continuing breach of that contract.

Exclusion may have the ancillary benefit of deterring providers of items or services from engaging in the same or similar misconduct as that engaged in by excluded providers. See Keszler at 33. However, the primary purpose of an exclusion is the remedial purpose of protecting the trust funds and beneficiaries and recipients of those funds. Deterrence cannot be a primary purpose for imposing an exclusion. Where deterrence becomes the primary purpose, section 1128 no longer accomplishes the civil remedies objectives intended by Congress. Punishment, rather than remedy, becomes the end.

> [A] civil sanction that cannot fairly be said solely to serve a remedial purpose, but rather can be explained only as also serving either retributive or deterrent purposes, is punishment, as we have come to understood the term.

United States v. Halper, 490 U.S. 435, 448 (1989).

Therefore, in order to be adjudged reasonable under section 1128, an exclusion must satisfy the remedial objective of protecting federally-funded health care programs and their beneficiaries and recipients from untrustworthy providers of items or services. An exclusion which satisfies this purpose may also have the ancillary benefit of deterring wrongdoing; however, that ancillary benefit will not sustain an exclusion where the exclusion does not reasonably serve the Act's remedial objective.

The I.G. argues that Congress intended that individuals and entities who are found to have committed acts in the nature of criminal offenses related to federally-funded health care programs should be excluded for substantial periods. As a general proposition, I agree that inferences as to parties' trustworthiness can be drawn from the conduct that they are found to have committed. In most circumstances, where a party is found to have committed misconduct in the nature of a program-related crime, the inference can be drawn that that party is untrustworthy and should be excluded. See Keszler at 38; Tommy G. Frazier and Prater Drugs, DAB Civ. Rem. C-127 at 23 (1990); Anesthesiologists Affiliated et al. and James E. Sykes, D.O., et al., DAB Civ. Rem C-99, C-100 at 58 (1990).

Furthermore, Congress has determined that parties who are convicted of crimes related to the delivery of an item or service under Medicare or Medicaid must be excluded for at least five years. Social Security Act, sections 1128(a)(1), (c)(3)(B). Had Respondents Hanlester, Omni, PPCL, and Placer been convicted of violating section 1128B(b)(2) in a criminal proceeding, then arguably they would have been convicted of a program-related crime, and the I.G. would have had no choice but to exclude them for at least five years. Given this, the mandatory exclusion provisions of sections 1128(a)(1) and (c)(3)(B) must be considered guidance as to what would comprise a reasonable exclusion for individuals and entities who are found in a civil remedies proceeding to have engaged in conduct which is in the nature of a program-related crime.

Guidance in measuring the reasonableness of an exclusion is also found in regulations contained in 42 C.F.R. Part 1003. These regulations apply to exclusions imposed pursuant to the Civil Monetary Penalties Law, Social Security Act section 1128A, and are not specifically applicable to cases under section 1128B. However, they express the Secretary's policy as to exclusions in circumstances which are not distinguishable from the present cases. Therefore, these regulations must be considered as nonbinding guidelines.[25] These regulations enumerate a number of factors which should be considered in deciding whether to impose an exclusion, and in deciding how long an exclusion should be. They include: the nature of the conduct which resulted in a finding of violation, 42 C.F.R. 1003.106(b)(1); the degree of culpability manifested by a party, 42 C.F.R. 1003.106(b)(2); whether a party has a prior history of offenses, 42 C.F.R. 1003.106(b)(3); the party's financial condition, 42 C.F.R. 1003.106(b)(4); and other matters as justice may require, 42 C.F.R. 1003.106(b)(5).

I conclude from applying all of these criteria and guidelines to the facts of these cases that no remedial purpose would be served by imposing exclusions against Respondents Hanlester, PPCL, Omni, and Placer. The offenses which I have found in these cases are of a nature that would ordinarily support an exclusion, and indeed, might mandate one if Respondents Hanlester, PPCL, Omni, and Placer had been convicted of a criminal offense pursuant to section 1128B(b)(2). However, there are unique circumstances here which preponderate against imposing an exclusion. The evidence establishes that these Respondents' liability emanates entirely from the misconduct of one individual, Ms. Hitchcock. These Respondents were demonstrably untrustworthy so long as Ms. Hitchcock represented them. The problems created by Ms. Hitchcock's agency, and Respondents' untrustworthiness, ended when Respondent Hanlester and Ms. Hitchcock parted company. No legitimate end would now be served by excluding Respondents Hanlester, PPCL, Omni, and Placer more than two years after their relationship with Ms. Hitchcock ended.

I would reach a different conclusion concerning the need for exclusions in these cases if I determined that Respondents manifested a propensity for hiring untrustworthy agents and employees, or that Respondents were indifferent to the consequences of their agents'

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[25] There are proposed regulations which, if adopted by the Secretary, would establish his policy for exclusions imposed pursuant to section 1128. See 55 Fed. Reg. 12205 (April 2, 1990). These proposed regulations have not been adopted. It would not be appropriate for me to consider them as guidelines, because they may not be finally adopted in their current form. Additionally, it is not clear that, assuming these proposed regulations are adopted, they would apply retroactively to exclusion cases heard prior to the date of their adoption.

acts. However, the evidence shows that Respondents Hanlester, PPCL, Omni, and Placer were concerned that their agents not make improper representations. Mr. Apprehamian repeatedly counseled Ms. Hitchcock not to make representations beyond what was contained in the private placement memoranda for Respondents PPCL, Omni, and Placer. That counseling was reinforced by Respondents Lewand and Tasha. Eventually, Respondent Lewand concluded that Ms. Hitchcock was uncontrollable. He had determined to discharge her when she resigned.

Application of the regulatory principles of 42 C.F.R. 1003.106 to these cases suggests that there is no need for exclusions here. The conduct of Respondents Hanlester, PPCL, Omni, and Placer which is the basis for my finding that section 1128B(b)(2) was violated is attributable to one individual, Ms. Hitchcock. This conduct was contrary to Respondents' intent and their policy. See 42 C.F.R. 1003.106(b)(1). Respondents, as distinguished from their agent, Ms. Hitchcock, manifest little culpability. See 42 C.F.R. 1003.106(b)(2). None of Respondents has a history of prior offenses. See 42 C.F.R. 1003.106(b)(3).[26]

There is no evidence that Respondents Hanlester, PPCL, Omni, or Placer caused harm to the Medicare or Medicaid programs. See 42 C.F.R. 1003.106(b)(5). Bribes, kickbacks, rebates, and other forms of proscribed remuneration carry the potential for substantial harm to federally-funded health care programs and to beneficiaries and recipients. Such unlawful inducements may encourage providers to order unnecessary items or services in order to obtain remuneration. Unlawful inducements may also cause providers to make choices which are not in the best interests of, and which are even potentially harmful to, persons whom they are entrusted to treat. The

[26] Respondents offered evidence to show that their interpretation of the Act is consistent with that advocated at times by various commentators including Departmental officials. The purpose of this evidence is to prove that Respondents believed that their conduct was legal. From this, Respondents argue that they are not untrustworthy health care providers. I make no findings as to this evidence because I conclude that the I.G. did not prove that Respondents Lewand, Tasha, Welsh, Huntsinger, and Keorle violated the Act and because I conclude that Respondents Hanlester, PPCL, Omni, and Placer are not untrustworthy for the reasons I cite in the body of this Decision.

potential for such harm is one of the principal reasons Congress enacted section 1128B. However, there is no evidence in this case to prove such harm actually resulted from the limited partners' participation in Respondents PPCL, Omni, and Placer. For purposes of deciding a remedy, I am not prepared to find the presence of harm based solely on the potential for such harm.

CONCLUSION

For the reasons set forth in this Decision, I conclude that Respondents Hanlester, PPCL, Omni, and Placer knowingly and willfully offered remuneration to physicians to induce them to refer program-related business in violation of section 1128B(b)(2) of the Act. I conclude that the I.G. did not prove that Respondents Lewand, Tasha, Welsh, Huntsinger, or Keorle knowingly and willfully offered or paid remuneration to physicians to induce them to refer program-related business in violation of section 1128B(b)(2) of the Act. I conclude that the I.G. did not prove that any of Respondents solicited or received remuneration in return for referring program-related business in violation of section 1128B(b)(1) of the Act. Finally, I conclude that no legitimate remedial purpose would be served by excluding Respondents Hanlester, PPCL, Omni, and Placer from participating in Medicare or Medicaid.

/s/

Steven T. Kessel
Administrative Law Judge