CLIENT ALERT

Federal Court Rules Hospitals Contracting with FEHBP HMO are "Subcontractors" Subject to Federal Affirmative Action Requirements

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Judge Paul Friedman of the United States District Court for the District of Columbia recently affirmed a determination by the U.S. Department of Labor (DOL) Administrative Review Board (ARB) that three hospitals that contracted with a health maintenance organization (HMO) were federal subcontractors under the HMO's contract with the United States Office of Personnel Management (OPM) to provide medical services and supplies to federal employees. *UPMC Braddock v. Harris,* No. 1:09-cv-01210-PLF (D.D.C. Mar. 30, 2013).As a result, the court found the hospitals were required to comply with affirmative action requirements for government contractors and subcontractors and subject to audit by DOL's Office of Federal Contract Compliance Programs (OFCCP). Judge Friedman's long-awaited decision has broad implications for health care providers, including those that hold contracts with HMOs who, in turn, hold contracts with certain federal health care programs, even when the provider-HMO contract makes no reference to any government contracting obligations. His decision also has significant implications for companies outside the health care industry if they enter into contracts with prime federal contractors, unaware that they are providing goods or services that will be used to satisfy government contracts. Under Judge Friedman's analysis, such companies would – unknowingly – be subject to affirmative action obligations and the OFCCP's jurisdiction.

Background

Plaintiffs were three hospitals affiliated with the University of Pittsburgh Medical Center (together, the "hospitals"). The hospitals had contracts with UPMC Health Plan (the "Health Plan") to provide medical services and supplies to plan beneficiaries. The Health Plan subsequently contracted with OPM to provide coverage for federal employees pursuant to the Federal Employees Health Benefits Program. DOL concluded that the hospitals were government subcontractors based on the OPM contract and subject to statutory and regulatory affirmative action requirements for government contractors and subcontractors. The hospitals appealed an ARB ruling that enjoined them from failing or refusing to comply with federal equal opportunity provisions.

Applicable Statutes and Regulations

All applicable government contracts and subcontracts, unless expressly exempted by rules, regulations, or orders of the Secretary of Labor (the "Secretary"), are required to include specific clauses that prohibit discrimination and require affirmative action in hiring and employment. *See* Section 503 of the Rehabilitation Act of 1973, as amended 29 U.S.C. § 793 ("Rehabilitation Act"), Section 402 of the Vietnam Era Veterans' Readjustment Assistance Act of 1974, 38 U.S.C. § 4212 (VEVRAA), and Executive Order 11246, 30 Fed. Reg. 12319 (Sept. 24, 1965).

The Secretary has issued regulations implementing the anti-discrimination and affirmative action requirements of the statutes and the Executive Order. The implementing regulations provide that the equal opportunity clauses are incorporated in all

qualifying contracts and subcontracts by operation of law, regardless of whether they are expressly included in the agreements. 41 C.F.R. § 60-1.4(e) (implementing Exec. Order No 11246); *see* 41 C.F.R. § 60-741.5(e) (implementing the Rehabilitation Act); 41 C.F.R. § 60-250.5(e) (implementing VEVRAA).

OFCCP enforces compliance, primarily through compliance evaluations ("audits") and investigations. During OFCCP audits and investigations, government contractors and subcontractors must permit access to their records and sites of employment and supply information as required by the Executive Order and by the rules, regulations, and orders of the Secretary. Exec. Order 11246 § 205.

Court Rules that the Health Plan and OPM Could Not Circumvent the Regulatory Definition of "Subcontractor"

The district court rejected the hospitals' argument that they were exempt from the affirmative action obligations because they were not "subcontractors" within the meaning of the OPM contract. Specifically, the district court held that the Health Plan and OPM could not contract around the statutory requirements or Executive Order 11246 by excluding providers of medical services and supplies from its contractual definition of a "subcontractor." The court noted that the Secretary has the sole authority to administer the statutes and Executive Order and to issue implementing regulations, and the sole authority to waive the non-discrimination or affirmative action requirements thereunder. Neither the OPM nor the Health Plan could adopt a narrower definition of "subcontractor" than the definition adopted by the Secretary. Nor could they independently waive non-discrimination and affirmative action requirements.

Court Finds the Hospitals Met the Regulatory Definition of a "Subcontractor" by Providing "Nonpersonal Services"

The district court also upheld the ARB's determination that the hospitals' agreements with the Health Plan qualified as "subcontracts" under the regulations implementing the equal opportunity requirements of Section 503 of the Rehabilitation Act, Section 402 of VEVRAA, and Executive Order 11246.

The implementing regulations define a "subcontract" as any agreement or arrangement between a contractor and any person (in which the parties do not stand in the relationship of an employer and employee):

> (1) For the purchase, sale or use of personal property, or for nonpersonal services, which, in whole or in part is necessary to the performance of any one or more contracts; or
> (2) Under which any portion of the contractor's obligation under any one or more contracts is performed, undertaken or assumed.

21 C.F.R. § 60-1.3; *see* 41 C.F.R. § 60-(*l*) (setting forth same definition); 41 C.F.R. § 60.250.2(*l*) (same).

While there is little case law interpreting these key regulatory provisions, the district court held that the hospitals satisfied the first prong of the regulation because they provided certain "nonpersonal services" that were "necessary to the performance" of the Health Plan's contract with OPM. To construe the term "nonpersonal services," Judge Friedman turned to a provision of the Federal Acquisition Regulations (FAR) – not a provision of the OFCCP's regulations – that defines a "nonpersonal services contract" as "a contract under which the personnel rendering the services are not subject, either by the contract's terms or by the manner of its administration, to the supervision or control usually prevailing in relationships between the Government and its employees." 48 C.F.R. § 37.101. Such contracts are characterized by the employer-employee relationship it creates between

the government and the contractor's personnel. 48 C.F.R. § 37.104(a). The district court held that the hospitals provided nonpersonal services because the hospital personnel were not in an employer-employee relationship with the Health Plan nor under the supervision and control that an employer would exercise over its employees.

Determination that the Hospitals Were "Necessary to the Performance" of the Health Plan's Contract with OPM

Third, the district court held that the hospitals were subcontractors because their services were "necessary to the performance" of the Health Plan's contract with the OPM and/or the hospitals' agreement with the Health Plan performed, undertook, or assumed a portion of the Health Plan's obligations under the OPM contract. 41 C.F.R. § 60-1.3; 41 C.F.R. § 60-741.2(*l*); 41 C.F.R. § 60-250.2(*l*).

The court distinguished *OFCCP v. Bridgeport Hosp.*, ARB Case No. 00-034 (Jan. 31, 2003), in which the ARB held that the hospitals at issue were not government subcontractors, because the OPM contract in *Bridgeport* obligated the health plan to provide health insurance but made no commitment to assure hospital care or services to enrollees. The plan's sole obligation was to provide reimbursement to policy holders for medical costs.

In this case, the Health Plan was an HMO, and under the OPM contract, the HMO agreed to provide medical services to federal employees by contracting with hospitals and providers to provide benefits, including medical services. The district court found that the provision of medical services and supplies was a critical component of the Health Plan's contract with OPM. Thus, the Health Plan's performance under the OPM contract depended upon medical providers like the hospital offering medical services and supplies, and the regulatory definition of "subcontractor" was satisfied. In distinguishing *Bridgeport*, the court did not discuss the statutory requirement for the service benefit plan in *Bridgeport* to also provide a network for the delivery of health care. See 5 U.S.C. § 8903(1) ("plan offering . . . benefits, under which payment is made by a carrier under contracts with physicians, hospitals, or other providers of health services").

Judge's Decision that the Hospitals Need Not Consent to Equal Opportunity Provisions to be Bound

Finally, the district court rejected the hospitals' contention that they did not consent to be bound by the affirmative action requirements of Executive Order 11246, the Rehabilitation Act, or VEVRAA because their agreements with the Health Plan did not include those clauses and gave no indication that the hospitals would become government subcontractors.

The court noted that under the "*Christian* Doctrine," "a mandatory contract clause that expresses a significant or deeply ingrained strand of public procurement policy is considered to be included in a contract by operation of law." *See G.L. Christian & Assoc. v. U.S.*, 312 F.2d 418, 424 (Ct. Cl. 1963). Under the *Christian* Doctrine, Judge Friedman ruled, a subcontractor's express knowledge of and consent to the affirmative action obligations is not required for it to be bound by the statutory and regulatory obligations imposed on federal contractors and subcontractors, and the government can compel a subcontractor to comply with the equal opportunity obligations of Executive Order 11246. Though the *Christian* Doctrine has historically been applied only to prime government contractors, who are fully aware of their contracting relationship with the federal government, Judge Friedman found there was no basis on which to refrain from applying the doctrine to subcontractors who lack knowledge that they are providing services that may subject them to affirmative action obligations. Instead, he found a subcontractor may be similarly bound if it helps the contractor to fulfill its agreement with the government, thereby reaping the financial benefit of that agreement.

The district court concluded that constructive knowledge of the regulations could be imputed to the hospitals based upon the payments of $500,000 or more that each hospital received during the relevant time period. Moreover, the agreements under which the hospitals received such payments met the definition of a "subcontract" under the Secretary's regulations and FAR.

Who Does this Decision Affect?

The district court's opinion in *UPMC Braddock* will, if it stands, affect a broad range of health care providers. Those health care providers that have contractual arrangements with health plans, which, in turn, have HMO contracts with the Federal Employees Health Benefits Program (FEHBP), would be subject to OFCCP's jurisdiction. It will remain to be seen what position OFCCP takes with respect to health care providers associated with other federal managed care programs, such as Medicare Part C (Medicare Advantage) and Part D (Prescription Drug Programs).

The decision should not have significance for health care providers furnishing medical services to TRICARE beneficiaries, due to recent legislation that expressly exempts them from OFCCP jurisdiction. The full reach of that exemption is not yet resolved. Also, in light of earlier-issued OFCCP guidance and differences in the structure and relationships involved, the decision also should not raise concern that health care providers under Medicare Part A and Part B and Medicaid will, by virtue of that status, be deemed subcontractors.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

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