California Appeals Court Says Hospitals Must Prove Charges are Market Rates when Collecting from Non-Contracted Parties

The Overview

Last month, a California appeals court struck a blow to hospitals' charging the rates included in their chargemasters in non-contract situations. Children's Hospital of California sued Blue Cross of California, demanding that the insurer pay the full chargemaster rates for services rendered outside of a contract. Blue Cross claimed that, under California regulations governing claims settlements, it only owed the Hospital the reasonable value of the services, which it calculated as rate paid by the government. In 2012 the lower court in Madera County agreed with the Hospital and ruled that Blue Cross must pay the balance of its bill. However, last month, Judge Levy of the California Court of Appeals, 5th Appellate District, reversed, ruling that the insurer need only pay the "reasonable value" which meant the "market value" of the services. The court reached its conclusion by (1) interpreting California Code of Regulations Title 28, Section 1300.71, a claims settlement regulation authorized by the California Health and Safety Act and effected by the Department of Managed Health Care, which imposes procedural requirements on claim processing, and (2) applying the more general rule that, when operating outside a contract, one who provides services is entitled to be paid what is *deserved*—not just what he or she claims to be owed. In other words, hospitals now have to play by the same rules that everyone else follows when billing for their services by showing that their charges are reasonable.

In ruling for Blue Cross, the Court of Appeals articulated what most of us understand to be true about chargemaster rates – "a medical care provider's billed price for particular services is not necessarily representative of either the cost of providing those services or their market value." Instead, those charges are just what

the hospital claims the services are worth (… sometimes—usually hospitals are willing to accept less). In fact, providers often acknowledge that those rates are much higher than market rates. Certainly, contracted rates with insurers and governments are typically fractions of the full rates, and an oft-heard refrain of those maintaining the inflated charge masters is that "nobody pays the full charge." Well, that may be true now in California. As the folk wisdom says, "something is only worth what someone is willing to pay for it," and hospitals will now have to attempt to prove that someone is willing to pay the chargemaster rates if that is what they continue to bill insurers or patients in non-contract situations.

The appeals court's ruling sent the case back to the trial court. However, on July 17, Children's Hospital petitioned the California Supreme Court to hear the case, arguing that the ruling "disrupts the carefully established balance between plans and providers during contract negotiations," and that it "will have a profound and fundamental impact on the way in which health care is delivered to patients in California." The hospital warned that the ruling would give plans and providers less incentive to enter into contracts that benefit consumers. It remains to be seen whether the state's high court will take the case, and, if so, whether it will agree.

The Facts

Interactions between Children's Hospital and Blue Cross operate under various contracts, but in this instance, the applicable contract had lapsed for a ten-month period. The dispute concerned services provided to patients enrolled in the Medi-Cal managed care plan, under which the California Department of Health Care Services ("DHCS") pays a monthly fixed fee per patient to Blue Cross. In turn, when services are rendered for Medi-Cal managed care, Blue Cross pays the Hospital. The services at issue were part of "post-stabilization care," which, unlike emergency care, is not mandated by state and federal law, and may require pre-authorization by a health plan for reimbursement. For mandated emergency care, the Hospital is required by law to accept from Blue Cross the amount it would receive directly from DHCS for those services—the average California Medical Assistance Commission ("CMAC") rate. When the Hospital billed Blue Cross for the emergency *and* post-stabilization services, Blue Cross paid the CMAC rate for both types of services. The Hospital then brought a claim for additional moneys for the post-stabilization services,

requesting the difference between the CMAC rate and the chargemaster rate. When the Hospital claimed that the "reasonable and customary value" of the services it provided was equal to the amount billed via the chargemaster, the court disagreed.

The Law

For a comprehensive summary of the court's reasoning, read our case summary. In brief, it came down to this: The law allows parties who provide a service for which they are not paid to sue for payment, and to prove to a court what they are owed in an age-old remedy called *quantum meruit*, or "what one has earned." The California Appeals court has made clear that hospitals, just like other entities and persons, are subject to this timeless concept that is based in fairness. The Hospital relied on a claims settlement regulation, which it essentially asserted as an exception to the rule|however, the court said that regulation was actually just an application of *quantum meruit* to health claims settlements. If hospitals want to obtain the full chargemaster rates outside of a contract, they have to show that they deserve them. The chargemaster is only one piece of evidence—the ceiling—for "reasonable" or "market value."

The Impact

It is clear that California hospitals must now expect to prove that what they bill for services is equal to the value of the services provided. What is unclear is how this case will affect how hospitals charge non-contracted parties in the first place. It may be that hospitals will lower their chargemaster rates to more accurately reflect market rates, if they are likely to face a losing court battle over inflated charges. It will be interesting to see how this plays out over time. This case is certainly a win for fairness in hospital pricing at the legal level, and is likely to have great practical effects as well.