To be argued
By: KATE H. NEPVEU
10 minutes requested

Supreme Court of the State of New York
Appellate Division – Third Department

In the Matter of the Application of

AARON MANOR REHABILITATION AND NURSING CENTER, LLC, ET AL.,

Plaintiffs-Petitioners-Cross Appellants,

v.

HOWARD A. ZUCKER, M.D., J.D., AS COMMISSIONER OF NEW YORK STATE DEPARTMENT OF HEALTH, ROBERT MUJICA, AS DIRECTOR OF THE BUDGET,

Defendants-Respondents-Appellants,

For a Judgment Pursuant to Article 78 of the Civil Practice Law & Rules.

No. 533802

BRIEF FOR DEFENDANTS-APPELLANTS

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PRELIMINARY STATEMENT

Before April 2020, the Medicaid reimbursement rate for proprietary nursing homes could include a discretionary factor known as the residual equity reimbursement factor. However, in the 2020-2021 Budget Law enacted on April 3, 2020, the residual equity reimbursement factor was eliminated, effective April 1, 2020. In August 2020, the New York State Department of Health notified nursing homes of the adjustments to their reimbursement rates mandated by this amendment.

Plaintiffs-Petitioners are nursing homes that challenged the elimination of the residual equity reimbursement factor by bringing this combined declaratory judgment action and article 78 proceeding against defendants-respondents, the Commissioner of the Department of Health and the Director of the Budget. By decision and order/judgment dated June 1, 2021, Supreme Court, Albany County (O'Connor, J.), granted the petition in part, holding that removing the factor as of April 1, 2020, was improperly retroactive in violation of Public Health Law § 2807(7).

The petition and complaint should be dismissed in its entirety. The retroactive adjustments to plaintiffs' reimbursement rates did not violate Public Health Law § 2807(7), because they were authorized—indeed,

required—by law. Because Supreme Court's erroneous reading of the statute defeats the Legislature's unambiguously expressed intent, the judgment below should be reversed to the extent that it granted plaintiffs relief.

QUESTION PRESENTED

Did the 2020-2021 Budget Law require retroactive adjustment of plaintiffs' Medicaid rates, where it directed that a payment factor be eliminated effective two days before the statute was enacted and notwithstanding any contrary provision of law?

Supreme Court answered in the negative.

STATEMENT OF THE CASE

A. Statutory and Regulatory Background

Medicaid is a joint state and federal program that funds medical services for the needy. 42 U.S.C. §§ 1396–1396w-6; Social Services Law §§ 363–369. The Department of Health is the single State agency responsible for the administration of the New York State Medicaid Program. 42 C.F.R. § 430.0; Public Health Law § 201(1)(v); Social Services Law § 363-a(1).

Residential health care facilities, referred to as RHCFs or nursing homes, are reimbursed by Medicaid through per diem rates set by the Department of Health. Public Health Law §§ 2807, 2808; 10 N.Y.C.R.R. subpart 86-2. The Department sets rates on a prospective basis, that is, in advance of the rate periods to which the rates will apply. Generally, the Department "shall notify" nursing homes of their rates "at least sixty days prior to the beginning of an established rate period for which the rate is to become effective." Public Health Law § 2807(7). However, advance notice is not required in all circumstances. For example, the notice period does not apply to rate adjustments that follow "judicial annulment or invalidation of previously issued rates," Public Health Law § 2807(7); that are based on audits or facilities' rate appeals, Public Health Law § 2808(11); or that are "otherwise authorized by law," *id.*

A facility's Medicaid rate consists of components tied to that facility's direct costs, indirect costs, noncomparable costs, and capital costs. 10 N.Y.C.R.R. § 86-2.10(a)(6)-(7), (b)(1)-(2). Capital costs, in turn, principally consist of interest on capital indebtedness and the cost of real property. *Id.* § 86-2.21(e). (Record on Appeal ["R."] 213 ¶ 7.) Proprietary nursing homes are reimbursed for the cost of real property through "a

payment factor sufficient to return equity." 10 N.Y.C.R.R. § 86-2.21(e)(4).[1] This factor is included in the facility's capital costs component during each year of useful facility life, which is a forty-year period beginning when the facility commences operations. *Id.* § 86-2.21(a)(7), (e)(1).

After a facility's useful facility life expires, the capital costs component of its rate no longer includes a return on equity. Before the 2020-2021 Budget Law, the Department Commissioner was permitted—but not required—to "approve a payment factor for any facility for which he determines that continued capital cost reimbursement is appropriate." 10 N.Y.C.R.R. § 86-2.21(e)(7). This payment factor, referred to as a residual equity reimbursement factor, could not "exceed one half of the capital cost reimbursement received by such facility in the final year of useful facility life." *Id.*

[1] Not-for-profit nursing homes are reimbursed for the cost of real property through allowable depreciation reported in their cost reports. 10 N.Y.C.R.R. § 86-2.19. (R. 213 ¶ 8.)

B. The 2020-2021 Budget Law

On April 3, 2020, the 2020-2021 Budget Law was enacted. L. 2020, ch. 56. (R. 105.) Part NN of section 1 made two changes to Medicaid reimbursement rates. First, it reduced by five percent the capital cost component for all nursing homes. L. 2020, ch. 56, § 1, Part NN, § 1; Public Health Law § 2808(2-b)(b)(iv). (R. 106.) That reduction is not at issue.

Second, it eliminated the residual equity reimbursement factor. Specifically, the Public Health Law now provides that

> Notwithstanding any contrary provision of law, rule or regulation … for rate periods on and after April first, two thousand twenty, there shall be no payment factor for residual equity reimbursement in the capital cost component of Medicaid rates of payment for services provided by residential health care facilities.

Public Health Law § 2808(20)(d); *see* L. 2020, ch. 56, § 1, Part NN, § 2 (adding material after ellipsis). (R. 106.)

The act specified that both provisions "shall take effect immediately and shall be deemed to have been in full force and effect on and after April 1, 2020." L. 2020, ch. 56, § 1, Part NN, § 3. (R. 106.) While the Director of the Budget was authorized to delay these effective dates, *id.*, he chose not to.

The Department complied with the new law by recalculating facility rates for a period beginning April 2, 2020, rates that were then approved by the Department's Medicaid Director and the Director of the Budget.[2] (R. 217 ¶ 14.) The Department also submitted a State plan amendment to the Centers for Medicare & Medicaid Services, as required by federal law. (R. 218 ¶¶ 15-16, R. 221; *see* R. 259 (CMS approval).) On August 7, 2020, after completing these necessary steps, the Department notified facilities of their reimbursement rates effective April 2, 2020, which, as mandated by the 2020-2021 Budget Law, eliminated residual equity reimbursements and reduced the capital component of the rates by five percent. (R. 244.)

C. Proceedings and Decision Below

Plaintiffs are proprietary residential health care facilities, some—but not all—of which had previously been eligible to receive a residual equity reimbursement factor because they had reached the end of useful

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[2] The rates subject to recalculation were effective on January 1, 2020, and had been provided to facilities sixty days in advance, on November 1, 2019. (R. 220.)

facility life.[3] (R. 286 ¶ 2, R. 295 ¶ 44.) They commenced this combined declaratory judgment action and article 78 proceeding on August 3, 2020 (R. 40, 44), arguing principally that the complete elimination of the factor violated Public Health Law § 2807(3), which requires that nursing homes' rates be certified as "reasonable and adequate to meet [their] costs," and their constitutional right to equal protection, because they were being treated differently from not-for-profit facilities. (R. 296 ¶ 50, R. 299 ¶ 65, R. 300 ¶¶ 78-79). However, they also argued that the adjusted rates were improperly retroactive to April 2020, because they did not receive 60 days' notice before the rates were effective. (R. 299 ¶ 71.)

Supreme Court granted plaintiffs a preliminary injunction that prevented defendants from taking any action to eliminate payment of the residual equity factor. (R. 266, 281.) Defendants appealed,[4] but final judgment was entered before the appeal was heard, and thus the appeal was withdrawn.

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[3] For the sake of brevity, this brief will refer to "plaintiffs" to mean those facilities that have reached the end of their useful facility life. Defendants challenged the standing of the other facilities in Supreme Court, which declined to reach the issue. (R. 25-26.)

[4] Defendants also moved for leave to reargue, which was ultimately denied. (R. 19.) That is not at issue here.

In the appealed-from final judgment, Supreme Court dismissed the petition and complaint except as to the retroactivity claim. Regarding the Public Health Law § 2807(3) claim, it concluded that plaintiffs "have not shown, by any competent evidence, that their rates would be inadequate to cover their necessary, as opposed to actual, costs" once the residual equity factor is eliminated. (R. 29.) Nor had they shown that rates would be inadequate for "efficiently and economically operated facilities" generally. (R. 30.) Supreme Court further dismissed plaintiffs' equal protection claim because proprietary facilities were not similarly situated to not-for-profit facilities. (R. 30.)

Supreme Court did conclude, though, that eliminating the residual equity reimbursement factor retroactive to April 2020 was inconsistent with Public Health Law § 2807(7)'s advance notice requirement. (R. 28.) It acknowledged (R. 31) that Public Health Law § 2808(11) explicitly provides that section 2807(7) "shall not apply to prospective or retroactive adjustments to rates … as otherwise authorized by law." But it rejected defendants' argument that retroactive adjustments were "authorized by law" within the meaning of section 2808(11) "simply because they are authorized by an act of the Legislature." (R. 34.) It noted that section

2808(11) had been enacted in response to a perceived flaw in section 2807(7), citing *Matter of Jewish Home & Infirmary of Rochester v. Commissioner of N.Y. State Dept. of Health*, 84 N.Y.2d 252 (1994). (R. 33.) It thus concluded that section 2808(11) *only* authorized retroactivity in the specific situation that prompted its enactment (R. 33-34), despite its unqualified language.

Supreme Court also recognized that the Legislature had eliminated residual equity reimbursement "for rate periods on and after April first, two thousand twenty," and had done so "[n]otwithstanding any contrary provision of law, rule or regulation." Public Health Law § 2808(20)(d). (R. 35.) However, it was "not persuaded" that the "notwithstanding" provision invalidated the advance notice requirement, theorizing that if the Legislature had "intended retroactive application," it "would have expressly provided for an exception" to that requirement. (R. 35.) It accordingly declared that "any change to plaintiffs-petitioners' Medicaid reimbursement rates to remove residual equity reimbursement, in accordance with Public Health Law § 2808[20](d), back to April 1, 2020 is improperly retroactive and violative of PHL § 2807(7)," and barred

defendants "from taking any action to implement the residual equity elimination clause retroactively back to April 1, 2020." (R. 37.)

This appeal and cross-appeal followed.

ARGUMENT

THE RETROACTIVE ADJUSTMENTS TO PLAINTIFFS' MEDICAID REIMBURSEMENT RATES WERE REQUIRED BY STATUTE

Contrary to Supreme Court's findings, the unambiguous text of the 2020-2021 Budget Law required the retroactive elimination of the residual equity reimbursement factor. Further, this retroactivity is consistent with the statutory framework and with decades of precedent permitting the Legislature to authorize such adjustments. The judgment below should thus be reversed to the extent it granted the petition and complaint.

Supreme Court misconstrued the 2020-2021 Budget Law when it held that the Legislature had not expressly provided for an exception to section 2807(7)'s advance notice requirement. (R. 35.) Rather, three separate elements of the statute demonstrate the Legislature's intent to retroactively eliminate the residual equity reimbursement factor. First, the Legislature prohibited payment of the reimbursement factor "for rate

periods on and after April first, two thousand twenty," despite the fact that the amendment was not enacted until April 3, 2020. Public Health Law § 2808(20)(d); *see* L. 2020, ch. 56, § 1, Part NN, § 2. (R. 106.) Second, it did so "[n]otwithstanding any contrary provision of law, rule or regulation," Public Health Law § 2808(20)(d), thereby setting aside the advance notice requirement of Public Health Law § 2807(7). Third, it directed that the law "shall be deemed to have been in full force and effect on and after April 1, 2020," that is, that it had retroactive effect. L. 2020, ch. 56, § 1, Part NN, § 3. (R. 106.) Any one of these might have sufficed to demonstrate the Legislature's intent that plaintiffs' rates be retroactively adjusted; the combination of all three puts the matter beyond question. In other words, though Supreme Court purported to rely on "the plain language" of the amended section 2808(20)(d) when granting relief to plaintiffs (R. 35), in fact it rejected the plain language of that section and its accompanying effectiveness clause. Its erroneous reading frustrates the Legislature's express and unambiguous intent to eliminate the residual equity reimbursement factor as of April 1, 2020, and therefore it must be reversed.

Supreme Court seems to have taken an unduly broad view of the advance notice requirement in Public Health Law § 2807(7) based on its misinterpretation of the Court of Appeals' decision in *Matter of Jewish Home & Infirmary of Rochester v. Commissioner of N.Y. State Dept. of Health*, 84 N.Y.2d 252 (1994). (R. 33.) In that case, the Court of Appeals considered whether the advance notice requirement applied to rates that had been judicially nullified, or only to, as the Department argued, rates created in the "normal rate-making process." 84 N.Y.2d at 260. The Court rejected the Department's argument, relying in part on the legislative history of section 2808(11); it noted that in enacting section 2808(11), the Legislature had been aware of the controversy at issue in the present litigation, but had expressly declined to resolve it. 84 N.Y.2d at 263. The Court thus concluded that the Department could not "attempt[ ] to circumvent the legislative process by invoking the judiciary's power to construe an existing statute." *Id.*[5]

The Court of Appeals' decision in *Jewish Home* was not—as Supreme Court interpreted it—a sweeping statement that Public Health

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[5] Public Health Law § 2808(11) was subsequently amended to apply to rates that had been judicially nullified. L. 1996, ch. 474, § 210.

Law § 2808(11) permits only retroactive rate changes that were individually and specifically negotiated by industry officials and the Department of Health in the lead-up to section 2808(11)'s enactment. (*See* R. 33.) Rather, the Court of Appeals concluded that the Department was attempting to make a rate adjustment that the Legislature had specifically declined to adopt. 84 N.Y.2d at 263. It was that conclusion, and not any special status ascribed to sections 2807(7) or 2808(11), that prompted the holding in *Jewish Home*.

Indeed, the advance notice requirement in section 2807(7) is part of a larger statutory framework, like that of any other statute. *See Terence Cardinal Cooke Health Ctr. v. Commr. of Health of the State of N.Y.*, 175 A.D.3d 435, 436 (1st Dep't 2019) (holding that the plaintiff was not entitled to 60-day notice period because it was specialty hospital to which section 2807(7) did not apply). And for decades, courts have recognized that the statutory framework may contemplate, and thus authorize, retroactive adjustments to Medicaid rates.

For instance, in 1983, the Court of Appeals affirmed this Court's holding that the Department "may retroactively readjust plaintiff's reimbursement rates." *Tioga Nursing Home v. Axelrod*, 90 A.D.2d 570,

571 (3d Dep't 1982), *aff'd*, 60 N.Y.2d 717 (1983). The plaintiff in that case challenged a retroactive revision that accounted for the actual, rather than the estimated, cost of obtaining a mortgage. 90 A.D.2d at 571. This Court upheld the revision, noting that reimbursing the higher estimated cost would "defeat the purpose" of the statute, which was to reduce the costs of care by authorizing less expensive mortgages. *Id.* at 572. As the Court of Appeals recognized in affirming this Court's decision, then, "[a]djustments to an established rate that are contemplated by the statutory reimbursement scheme do not constitute impermissible retroactive rate-making." *St. Joseph's Hosp. Health Ctr. v. Department of Health of State of N.Y.*, 247 A.D.2d 136, 146 (4th Dep't 1998) (citing *Tioga Nursing Home*, 90 A.D.2d at 571), *lv. denied*, 93 N.Y.2d 803 (1999).

Following this precedent, this Court recently upheld the retroactive application of a Department program, known as the Nursing Home Quality Pool, that reduced all facilities' Medicaid reimbursements to fund quality incentive payments to certain facilities. *Matter of Dry Harbor Nursing Home v. Zucker*, 175 A.D.3d 770, 771 (3d Dep't 2019). In 2014, the governing statute was amended to provide that regulations regarding the program "may be made effective for periods on and after January 1,

2013." *Id.* at 775 (quoting Public Health Law § 2808(2-c)(d) (alterations omitted)). This Court held that "[t]his statutory provision demonstrates that retroactive application of the Quality Pool [was] clearly intended" and, therefore, was proper. 175 A.D.3d at 775 (internal quotation omitted).

Similarly, as noted above, the Legislature here clearly intended retroactive elimination of the residual equity reimbursement factor. *See* Public Health Law § 2808(20)(d); L. 2020, ch. 56, § 1, Part NN, § 3. (R. 106.) Supreme Court failed to recognize that when a retroactive rate change has been, as it put it, "authorized by an act of the Legislature" (R. 34), then that change *is*, by definition, "authorized by law" and consequently exempted from the advance notice requirement under section 2808(11). It therefore erred in ordering declaratory and injunctive relief in plaintiffs' favor.

Finally, Supreme Court failed to recognize two other points about the statutory framework that support retroactive adjustment of plaintiffs' rates. First, even setting aside the text, such retroactivity was inevitable as a practical matter thanks to other statutory requirements, of which the Legislature is "presumed to be aware." *Arbegast v. Board of*

Educ. of S. New Berlin Cent. School, 65 N.Y.2d 161, 169 (1985). Rates must be certified by the Commissioner of the Department of Health and approved by the Director of the Budget. Public Health Law § 2807(3), (7). Further, this particular change had to be submitted for approval to the federal government. (R. 218 ¶¶ 15-16.) As a result, even if the statute had been enacted on April 1, 2020—instead of two days later—it would have been impossible for the revised rates to take effective immediately, rather than retroactively.

Second, the purpose of the Budget Law was to reduce State expenditures during a fiscal crisis, as shown by the accompanying across-the-board reduction in the capital cost component for all nursing homes. L. 2020, ch. 56, § 1, Part NN, § 1; Public Health Law § 2808(2-b)(b)(iv). (R. 106.) As in *Tioga Nursing Home*, it would defeat the purpose of the statute to prohibit these rate adjustments. 90 A.D.2d at 572. Supreme Court failed to recognize that the Legislature explicitly provided that these adjustments should take effect as of April 1, 2020, and thus should not have granted the petition and complaint to this extent.

CONCLUSION

The judgment below should be reversed to the extent that it granted plaintiffs declaratory and injunctive relief, and the combined action and special proceeding should be dismissed in its entirety.

Dated: Albany, New York
November 1, 2021

Respectfully submitted,

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