STATE OF MINNESOTA | DISTRICT COURT

COUNTY OF RAMSEY | SECOND JUDICIAL DISTRICT

Case Type: Other Civil

THE STATE OF MINNESOTA, | Court File C1-94-8565

BY HUBERT H. HUMPHREY, III,
ITS ATTORNEY GENERAL,

and

BLUE CROSS AND BLUE SHIELD
OF MINNESOTA,

Plaintiffs,

vs.

PHILIP MORRIS INCORPORATED,
R.J. REYNOLDS TOBACCO COMPANY,
BROWN & WILLIAMSON TOBACCO CORPORATION,
B.A.T. INDUSTRIES P.L.C.,
BRITISH-AMERICAN TOBACCO COMPANY LIMITED,
BAT (U.K. & EXPORT) LIMITED,
LORILLARD TOBACCO COMPANY,
THE AMERICAN TOBACCO COMPANY,
LIGGETT GROUP, INC.,
THE COUNCIL FOR TOBACCO RESEARCH - U.S.A., INC., and
THE TOBACCO INSTITUTE, INC.,

Defendants.

PLAINTIFFS' MEMORANDUM IN OPPOSITION TO DEFENDANTS' CONSOLIDATED MOTION FOR PARTIAL SUMMARY JUDGMENT ON CERTAIN DAMAGES ISSUES:

RECOVERY OF FEDERAL SHARE OF MEDICAID

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I. INTRODUCTION

Medicaid, first enacted by the U.S. Congress in 1965, is a means-tested entitlement program providing medical and long-term care to those who cannot afford health care owing to poverty, old age, or physical disability. Each state has its own Medicaid program, administered exclusively by that state. Cong. Research Serv., 103d Cong., 1st Sess., Medicaid Source Book: Background Data and Analysis, p. 1-26 (Comm. Print, 1993 Update). Ex. 1.[1]

Defendants' position is, that the State of Minnesota ("the State") is not entitled to recover the full damages it suffered at the hands of the defendants -- tobacco-attributable health care costs paid by the State to Medicaid providers -- on the grounds that the State was ultimately reimbursed a portion of those costs by the federal government.[2] Defendants' position flatly ignores both the fundamental principles of the Medicaid statutory scheme and the fact that the Minnesota Supreme Court has already ruled that the pass-through defense is not available to the defendants in this case. State of Minnesota v. Philip Morris Inc., 551 N.W.2d 490 (Minn. 1996).

This very same motion has been brought by the tobacco industry in both the Mississippi and Texas Medicaid cases. Both the Mississippi and Texas courts denied defendants' motion, permitting each state to seek recovery of the full extent of their damages. Ex. 2.

II. RECITAL OF DISPUTED FACTS AND STATEMENT OF SUPPORTING DOCUMENTS OF RECORD

Plaintiffs rely upon the Medicaid Source Book: Background Data and Analysis (1993), as well as the Affidavit of Kathleen Lee, Federal Funds Manager, Division of Financial Management, Department of Human Services, State of Minnesota, and all exhibits to the Affidavit of Susan Richard Nelson.

III. ARGUMENT

A. Medicaid Health Care Costs Are Paid To Medicaid Health Care Providers In Full By The State Which Then Receives Partial Reimbursement From The Federal Government

The full amount of Medicaid health care costs is drawn on the State account, using State funds, to pay

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[1] All exhibits are to the Affidavit of Susan Richard Nelson.

[2] This argument is part of defendants' consolidated motion for summary judgment "on certain damage issues." As this question presents a discrete legal issue unrelated to the other issues in defendants' motion, plaintiffs respond in this separate brief to the defendants' argument. See

Medicaid health care providers on a weekly basis. At a subsequent time, the State receives reimbursement for a portion of those funds from the federal government.

Minnesota Medicaid prepares warrants, or checks, for health care costs payable to health care providers for medical and long-term health care costs. Those checks represent the full amount of the costs of Medicaid health care. The checks are drawn on the State account and use State funds. Ex. 3, at ¶ 3 (Affidavit of Kathleen Lee).

The 1990 Cash Management Improvement Act, 31 U.S.C. § 6501 et seq., ("the 1990 Act"), regulations thereunder, 31 C.F.R. § 205 et seq., and agreements thereunder, define the specific protocol for receiving federal reimbursement for Medicaid and other programs. Minnesota is a party, under the 1990 Act, to an agreement each year entitled the "Treasury State Annual Cash Agreement" which further defines the method of receiving federal reimbursement for Medicaid and other programs. Ex. 3, at ¶ 4.

In accordance with the Treasury State Annual Cash Agreement in effect between Minnesota and the federal government, Minnesota is obligated to wait a certain number of days (currently three days) before it may obtain reimbursement from the federal grant award. Ex. 3, at ¶ 5. The "check clearance pattern" is an estimate of the average period of time it takes the check drawn on the State account, containing State funds, to reach the provider, be deposited and clear the bank. Only then, can the State of Minnesota draw down reimbursement from the federal grant award. Id. at ¶6. To do so, Minnesota uses the Federal Payment Management System in Rockford, Maryland ("FPMS"). FPMS keeps track of the "federal share net reimbursement" drawn down by the State each quarter. Id.

Defendants' description of the method of federal reimbursement of funds is inaccurate. (Defendants' Memorandum in Support of Defendants' Consolidated Motion for Partial Summary Judgment on Certain Damages Issues at 3-5).[3]

Under the Medicaid statutory scheme, the federal government awards "grants" of money to each State in accordance with a federally mandated formula, known as "Federal Financial Participation" ("FFP"). FFP is designed to provide financial assistance to states for Medicaid health care expenditures under a formula based on per capita

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October 20, 1997 Order, ¶ 5.

[3] For instance, defendants cite to 31 C.F.R. § 205.7 (1996) as the funding technique applicable in Minnesota. 31 C.F.R. §205.7 (1996) states: "Unless otherwise specified in a Treasury-State agreement, a State and a Federal Agency shall adhere to the following procedures . . ." (emphasis added). Minnesota has such a Treasury-State agreement which defines the

income. Ex. 4, at 467-495 (Medicaid Source Book: Background Data and Analysis); 42 U.S.C. § 1396 et seq. States must comply with certain legal obligations set forth in the Medicaid regulations in order to receive reimbursement for a portion of the funds states expend for medical and long-term care. 42 C.F.R. § 430.30 et seq. (1996).

B. A Condition Of Receiving Federal Funds Is The Affirmative Obligation On The Part Of The State Of Minnesota To Seek And Recover Medicaid Health Care Costs

Under the Medicaid statutory scheme, one of the conditions of receiving federal funds is the affirmative obligation on the part of the State of Minnesota to seek recovery of Medicaid health care costs incurred by the State from responsible parties. Examples include:

- Drug Manufacturers for drug rebates mandated by the Omnibus Budget Reconciliation Act of 1990 ("OBRA 90"), as a condition of coverage of their prescription drug products;
- Private Insurers Or Other Governmental Insurers under the coordination of benefits section of the statute and regulations, 42 C.F.R. § 433.138 et seq. (1996);
- Health Care Providers, whether as a result of error, overpayment, fraud or abuse, 42 C.F.R. § 433.300 et seq. (1996); and
- Liable Third-Parties under the third-party liability provisions of the statute and regulations, 42 C.F.R. § 433.135 et seq. (1996).

Any such monies recovered by the State of Minnesota from responsible parties must be reported to HCFA. After those payments are recovered by the State (or in certain instances prior to their recovery), and properly reported, the federal government is entitled, and will take a credit for its portion of its reimbursement, by reducing the subsequent quarter's grant award by the amount of those recoveries. 42 C.F.R. 430.30(d) (1996).

It is critical to note that the Medicaid statutory scheme requiring the State of Minnesota to recover such monies extends well beyond the subrogation third-party liability provisions of the statute.[4] The obligation extends to drug manufacturers, private insurers, governmental insurers and health care providers as well. Consistent with the statutory scheme, health care providers who receive an overpayment, by error, fraud or abuse, must pay, in full, to the State of Minnesota, all amounts which are owing, including that portion of the health care payment which is ultimately reimbursed by the federal government. Similarly, private insurers and/or governmental insurers, to the extent that private or governmental insurance policies are applicable, must pay to the State of Minnesota, in full, all

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reimbursement methodology.

[4] As fully described in Plaintiffs' Opposition to Defendants' Motion for Partial Summary Judgment on Plaintiffs' Non-Statutory Claims, § III.B., the statutory provision allowing subrogation

amounts which are owing, again including that portion of the health care payment which is ultimately reimbursed by the federal government. Drug manufacturers, who provide rebates to the State of Minnesota by law, must provide the full amount of that rebate to the State of Minnesota, including that portion of the rebate which is ultimately reimbursed to the federal government.

It is apparent, then, that defendants' proposal to deprive the State of its ability to carry out this legally mandated process would be antithetical to the law and to the longstanding fundamental core policies of the Medicaid scheme. Health care providers, private and governmental insurers, responsible third-parties and drug manufacturers cannot be heard to argue that they must only pay the State for a portion of health care costs owing. Nor can the tobacco industry be heard to argue that they be treated differently under the law than all others responsible for Medicaid health care costs.

C. The Minnesota Supreme Court Has Ruled That The Pass-Through Defense Is Unavailable To The Defendants

Defendants' argument that the State should be deprived of recovering its full damages on the grounds that it passed through some of those costs to the federal government by way of federal reimbursement, flies in the face of the Minnesota Supreme Court's ruling in State of Minnesota v. Philip Morris Inc., 551 N.W.2d 490 (Minn. 1996). There, the Court specifically held that the pass-through defense is not available to the tobacco industry defendants in this case.

In State of Minnesota defendants similarly argued that Blue Cross and Blue Shield of Minnesota lacked standing to recover smoking-attributable health care costs because it had passed-through those costs to its subscribers. The Supreme Court specifically rejected defendants' argument that plaintiffs were unable to recover damages that ultimately may have been reimbursed or paid by a non-party to the lawsuit:

> The argument that no injury has been suffered because costs were passed through one entity to customers, consumers or other entities usually arises in antitrust cases. It has been uniformly rejected in the courts, primarily on the theory that the injury is sustained as soon as the price, artificially raised for whatever reason, has been paid.

Id. at 496.

The Court concluded that "it was the intent of the Minnesota Legislature to abolish the availability of the

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is not the State's exclusive remedy by which medical costs can be recouped.

pass-through defense by specific grants of standing within statutes designed to protect Minnesota citizens from sharp commercial practices." Id. at 497. The Court unconditionally held that "the pass-through defense is not available to the tobacco companies." Id.

The Court further held that the pass-through defense was equally "untenable . . . outside the context of antitrust and laws related to regulated industry." Id. at 497 (citing Adams v. Mills., 286 U.S. 397, 405 (1932)). In Adams., plaintiffs, members of the Chicago Livestock Exchange, brought suit in federal court to enforce an order of the Interstate Commerce Commission for reparations based on unlawful overcharges for unloading livestock received at defendant's stockyard from approximately 174,000 different shippers. Defendants argued that plaintiffs were not allowed to recover the overcharges because subsequent refunds were received from accounts of the shippers. The United States Supreme Court held:

> In contemplation of law, the claim for damages arose at the time the extra charge was paid. . . . Neither the fact of subsequent reimbursement by the plaintiffs from funds of the shippers, nor the disposition which may hereafter be made of the damages recovered, is of concern to the wrong-doers. . . . The plaintiffs have suffered injury within the meaning of section 8 of the Interstate Commerce Act; and the purpose of that section would be defeated if the tortfeasors were permitted to escape reparation by a plea that the ultimate incidence of the injury was not upon those who were compelled in the first instance to pay the unlawful charge. . . .

286 U.S. at 407-08 (emphasis added) (citations omitted).

Similarly here, and especially in light of the compelling practice regarding other Medicaid reimbursement schemes, neither the fact of subsequent partial reimbursement by the federal government, nor the disposition which may hereafter be made of the damages recovered to the federal government, should be of any concern to the defendants here.[5]

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[5] Cases cited in Defendants' Memorandum are inapposite and fail to address the issues at hand. Those cases are primarily personal injury cases that stand for the general proposition that a plaintiff in a personal injury action should be made whole. Several of the cases involve a claim by the defendant that the jury award was excessive, which is of no relevance to this issue. See Vanderlinde v. Wehle, 274 Minn. 477, 144 N.W.2d 547 (1966); Hallada v. Great Northern Railway, 244 Minn. 81, 69 N.W.2d 673 (1955), cert. denied, 350 U.S. 874, overruled on other grounds, Busch v. Busch Construction, Inc., 262 N.W.2d 377, 379 (Minn. 1977). The remainder of defendants' cases address standing issues regarding the rights of third parties -- an issue which is not before this Court and has already been settled in State of Minnesota. For instance, defendants cite 19 James W. Moore, Moore's Federal Practice 3d § 205.02[2][d][i] (3d ed. 1997), which references the case of Singleton v. Wulff, 428 U.S. 106, 96 S.Ct. 2868, 49 L.Ed.2d 826 (1976) (where two physicians brought an action for injunctive relief and sought standing to challenge the unconstitutionality of a Missouri statute precluding Medicaid reimbursement for abortions that were not "medically indicated"); and State v. Gray, 413 N.W.2d 107 (Minn. 1987) (where the

III. CONCLUSION

Consistent with the core policies of the Medicaid statutory scheme and the uncontroverted law of this case that the pass-through defense is unavailable to the defendants, the State of Minnesota respectfully requests that this Court deny defendants' motion. The State has the right to full recovery of the Medicaid tobacco-attributable health care costs the State has paid and is duty-bound to administer under the law and the State Plan with the federal government.

Dated this 4th day of November, 1997.

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Minnesota Supreme Court held that the defendant, an individual charged with violation of the criminal sodomy statute after engaging in sex for pay with a male prostitute, had no standing to challenge the overbreadth of the statute as it might be applied to persons who might engage in noncommercial sodomy).

ATTORNEYS FOR BLUE CROSS AND BLUE SHIELD OF MINNESOTA