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Federal District Court Affirms U.S. Department of Labor's Position that Healthcare Providers Participating in HMOs for Federal Employees Are Subject to Federal Contractor Affirmative Action Requirements

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In a long-awaited decision, the U.S. District Court for the District of Columbia ruled that three hospitals that provide medical services through a Health Maintenance Organization (HMO) to individuals covered by the Federal Employees Health Benefits Plan (FEHBP) are subject to the Office of Federal Contract Compliance Program's (OFCCP) jurisdiction and reporting requirements. The decision affirms the Department of Labor's stance that subcontractor status and the corresponding affirmative action obligations are imposed as a matter of law regardless of whether any contract document affirmatively confers the obligation and/or makes representations to the contrary.

Background

The case, *UPMC Braddock, et al., v. Harris*, involves three hospitals (the Hospitals) affiliated with University of Pittsburgh Medical Center which entered into contracts with UPMC Health Plan (the Health Plan), an HMO, to provide medical services to individuals enrolled in its coverage program. In 1995, when the Hospitals originally entered into the contracts with the UPMC Health Plan, the Health Plan was not participating in the FEHBP. Several years later, in 2000, the Health Plan decided to enter into the arrangement with the FEHBP by contracting with the U.S. Office of Personnel Management (OPM). The federal court observed that "[a]lthough the hospitals' original agreements with the Health Plan were entered into before the Health Plan held a contract with the federal government, each hospital renegotiated and renewed its agreement with the Health Plan after the year 2000," but acknowledged that "none of the agreements between the hospitals and the Health Plan contain[ed] provisions obligating the hospitals to comply with Executive Order 11246, Section 503 of the Rehabilitation Act, or Section 402 of [Vietnam Era Veterans Readjustment Assistance Act (VEVRAA)]," — the laws and regulations that OFCCP enforces.

In January 2004, OFCCP informed the Hospitals that they had been selected for a compliance review. The Hospitals jointly refused to participate, arguing that they did not hold government subcontracts and thus were not subject to OFCCP's jurisdiction. OFCCP filed Department of Labor administrative complaints against the Hospitals in November 2006 and an Administrative Law

Judge (ALJ) issued summary judgment in favor of OFCCP. The Hospitals filed exceptions to the ALJ's recommended decision and order with the Administrative Review Board (ARB), which upheld the ALJ's decision. The Hospitals subsequently appealed the ARB's decision to federal district court, which again ruled in favor of OFCCP.

On appeal, the court rejected the Hospitals' four longstanding arguments in support of their position that they were not federal government subcontractors. The rejection of the fourth and final argument is perhaps most troubling, as it has implications for the United States business community at large. As such, it will be addressed first.

No Notice Argument Rejected

The Hospitals were greatly troubled by the complete absence of any notice to them that the contracts they were asked to sign could and did impose affirmative action obligations. The Hospitals never consented to being a contractor or subcontractor, and their contracts were completely silent in that regard. There was no "flow down" or notice from the direct contractor that OFCCP's regulations applied. The federal court held that "[b]ecause the government has the power to determine the conditions upon which it will contract for goods or services, '[a]greement to such conditions is unnecessary: where regulations apply and require the inclusion of a contract clause in every contract, the clause is incorporated into the contract, even if it has not been expressly included in a written contract or agreed to by the parties.'" Accordingly, the court found that OFCCP can compel a company to comply with federal affirmative action regulations applicable to contractors and subcontractors even though the company had not expressly consented to be bound by the executive order and despite the fact that the contract with the prime or direct contractor was silent as to such compliance obligations.

The takeaway from this part of the decision is that companies that do not affirmatively address and/or ascertain their status as potential federal subcontractors do so at their peril. This is especially true in healthcare and other industries that are largely funded through federal dollars. The reason, simply, is the money trail. Generally, OFCCP will not know which companies are federal subcontractors. But OFCCP has much more information, and a better chance at ferreting out a "subcontractor" when dealing with organizations that traditionally receive federal funds. In those cases, OFCCP knows the types of questions to ask to make this determination more readily. Therefore, industries that commonly receive federal funds from contract arrangements are less likely to avoid OFCCP scrutiny.

Other Arguments Rejected

The court also rejected the Hospitals' contention that they are not subject to OFCCP's jurisdiction because the OPM and the Health Plan expressly agreed that a provider of medical services is not a "subcontractor" within the meaning of their contract. The OPM/Health Plan contract specifically excludes "providers of direct medical services or supplies pursuant to the [Health Plan's] health benefits plan" from the definition of "subcontractor" because that is the definition that OPM published in its regulations dealing with these types of FEHPB contracts. In response, Secretary Harris argued that the Secretary of Labor has the authority to administer Executive Order 11246, Section 503 of the Rehabilitation Act, and Section 402 of the VEVRAA and to issue regulations implementing them. The implementing regulations include a definition for "subcontractor" that does not exclude healthcare providers. Thus, Secretary Harris argued that neither a federal contracting agency nor the Health Plan was empowered to narrow the definition of "subcontractor" and thus override the requirements of the aforementioned laws and executive order. The Court agreed with Secretary Harris' argument and held that the OPM/Health Plan contract's definition of "subcontractor" has no effect on whether the Hospitals may be considered federal subcontractors under the applicable laws.

The Hospitals' next argument was that they did not meet the definition of "subcontractor" under laws enforced by OFCCP, which define a subcontract as "an agreement…for the purchase, sale or use of personal property or nonpersonal services which, in whole or in part, is necessary to the performance of the any one or more contracts…" The Hospitals asserted that the business of supplying medical care is one offering "personal" rather than "nonpersonal" services and, therefore, does not fall within the implementing regulations' definition of "subcontract." The court rejected this argument, concluding that the agency's view that supplying medical care is a nonpersonal service was not plainly erroneous or inconsistent with the regulation, and therefore could not be rejected by the court in light of the substantial deference given to an agency's interpretation of its own regulations.

Finally, the Hospitals argued that their agreement with the Health Plan does not fit the definition of a "subcontract" because the services provided by the Hospitals are not "necessary to the performance" of the OPM/Health Plan contract. In making their argument, the Hospitals relied on the ARB's decision in *OFCCP v. Bridgeport Hospital*, ARB Case No. 00-034. In that case, OFCCP attempted to obtain jurisdiction over Bridgeport Hospital based on its medical services agreement with Blue Cross/Blue Shield (Blue Cross), which contracted with OPM to provide health insurance to federal government employees. OFCCP argued that Bridgeport Hospital provided a service "necessary to the performance" of Blue Cross' contract with OPM because it provided medical services to policy holders at a discounted rate. Bridgeport Hospital denied it was a federal government subcontractor, arguing that Blue Cross' contract with OPM did not obligate Blue Cross to provide medical services to Blue Cross' policyholders, only insurance. The ARB agreed with Bridgeport's position and held that Bridgeport was not a federal government subcontractor.

The *Braddock* court disagreed, however, with the Hospitals' assertion that the *Bridgeport* decision controlled, holding that because the Health Plan agreed to serve in the capacity of an HMO rather than a traditional insurer, it therefore agreed to provide medical services to federal government employees. In making the distinction between traditional insurers and HMOs, the court held that the Hospitals are, as a result, federal government subcontractors that must submit to OFCCP's jurisdiction.

The Practical Impact of this Decision

The *Braddock* decision is a significant development for healthcare providers and the contracting community at large. The immediate effect of *Braddock* is that healthcare providers that subcontract with HMOs doing business with the FEHBP must comply with Executive Order 11246 and its statutory counterparts. The *Braddock* decision reinforces that there are many potential bases upon which OFCCP may—and likely will—assert jurisdiction over hospitals and other healthcare providers. Thus, despite the 2012 National Defense Authorization Act's exemption of TRICARE providers from federal contractor/subcontractor affirmative action obligations and the ARB's affirmation of that exemption,[1] many hospitals and medical providers will continue to be viewed by OFCCP as federal contractors or subcontractors. OFCCP may rely on other types of contracts to assert jurisdiction, including contracts through Medicare Advantage or any direct contracts with federal agencies for healthcare services.[2] It is in fact likely that OFCCP will continue to aggressively assert jurisdiction over employers in the healthcare industry and will use contracts with an HMO to provide coverage to federal employees who participate in the FEHBP, as well as these other types of contracts, as bases for asserting jurisdiction over the employers in the healthcare industry.

At this point, the healthcare community's best hope for relief is legislation similar to the 2012 TRICARE legislation that would clarify whether healthcare providers that contract with HMOs that, in turn, contract with the FEHBP, must comply with Executive Order 11246 and its statutory counterparts. Unless that happens, healthcare providers that hold contracts similar to those in *Braddock* should be prepared to comply with OFCCP obligations.

With respect to the broader federal contracting community, *Braddock*'s holding that federal government agencies do not have the authority to alter the regulatory definition of "subcontractor" may have sweeping implications. Currently, some federal agencies are informing prospective retailers that they may not be subject to OFCCP's reporting requirements if they were to put stores on military bases because these arrangements are concession agreements, not contracts. According to *Braddock*, however, another agency's statement that a contractor is not subject to OFCCP obligations is meaningless if the regulations, as interpreted by OFCCP, indicate otherwise. Like the healthcare community, contractors at large should be wary of relying on such statements and should review the regulations to determine whether they could be subject to OFCCP jurisdiction.

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1 *See House and Senate Overrule OFCCP on TRICARE Subcontractors*, by Rob Wolff, Healthcare Employment Counsel, available at http://www.healthcareemploymentcounsel.com/2011/12/21/house-and-senate-overrule-ofccp-on-tricare-subcontractors/

2 The Department of Veterans Affairs and the Federal Bureau of Prisons are two agencies that commonly enter into direct contracts for healthcare services.