Practices liable when business subcontractors violate HIPAA

Practices have a difficult battle ahead when it comes to breaches thanks to the HIPAA “mega-rule.” You’re now responsible for HIPAA violations by your business associates and any subcontractors they use (MPCA 2/4/13).

The original HIPAA didn’t directly apply to either but the Health Information Technology for Economic and Clinical Health (HITECH) Act made business associates subject to the security rule and the privacy rule’s use and disclosures requirements.

But the Jan. 25 mega rule, implementing the HITECH Act, extended HIPAA further to business associates’ subcontractors and their subcontractors. That means a subcontractor you didn’t know existed can cause or suffer a security breach of your patients’ protected health information (PHI) and you, as the covered entity under HIPAA, will bear the fall out, including notifying patients and reporting it to HHS.

(SEE BUSINESS RELATIONS, P. 4)

Paid overpayments, settlements could be tax deductible

BY MARLA DURBEN HIRSCH

Paying a settlement or overpayment to the government or a payer is never pleasant. But there’s a silver lining — some of those payments can be deducted on your tax return.

In a pair of recent private letter rulings, the Internal Revenue Service (IRS) said physicians are allowed to deduct as business losses any payments that were made as returned overpayments or as settlements of payment disputes. The anonymous physicians behind the letters had wrongly billed both private and state payers for services, which was determined later, and faced separate legal actions for repayment, said attorney Leigh Griffith, with the Waller Law Firm in Nashville. (Read the private letter rulings at www.irs.gov/pub/irs-wd/1240007.pdf and www.irs.gov/pub/irs-wd/1240015.pdf.)

These physicians then repaid the claims settlement and asked the IRS if the payments qualified as losses and were therefore tax deductible — the agency said they were.

(SEE COMPLIANCE GRAB BAG, P. 5)
Not all payments qualify

The repayment of funds to a government or private payer is typically not deductible because it's usually considered a fine or penalty. Also, loss deductions aren't allowed if they're against federal or state public policy.

But the tax code allows taxpayers to deduct losses incurred in a trade or business or for transactions that were to yield a profit. That means recoupment or damages doctor's paid to a government or private payer in settlement — even if the activity causing the original payment to the physician was improper — may be deductible as a loss only if the payment being made had previously been included as income on the physician's prior tax return, according to the IRS.

"If the [provider] characterizes the payment for compensation, restitution or civil damages, it generally will be deductible," Griffith says.

That's true even if the payer originally characterized the overpayment as a fraud or even criminal and claimed penalties and damages. What's important is how the final agreement is worded and characterized, not how the original dispute characterized it, the IRS says.

In one of the rulings, New Jersey State agreed to a civil settlement agreement with a physician in exchange for dropping a criminal indictment. The IRS allowed that payment to be deducted from the physician's tax return because the consent agreement was for "restitution" as a condition of dismissal of the charges and aligned with state law.

"In the health care world today, if it's just a dispute but a person wants money back, he will call it 'billing fraud' to get your attention and to get you to settle," Griffith says.

Note: The tax deductibility of the payment is not absolute. You can't take the tax deduction if you're returning the payment as a fine or penalty, as opposed to "restitution." Also, you can't take the deduction if the payment is not directly related to a payment made to you, Griffith says. For example, a settlement payment to HHS' Office for Civil Rights for a HIPAA violation would not be tax deductible.

Plus, you can't take the deduction as a loss if you never declared it as income on your tax return to begin with, says attorney Pat Hintz, with Quarles & Brady in Milwaukee, Wis.

Take 4 steps before claiming payments on your tax return

Overpayments you return or settlement payments you make with a government or private payer may be tax deductible. However, those deductions must be taken with precaution; consider these steps first:

- **Review your situation to see if you may qualify to take the tax deduction.** Look at the tax and state laws and the private letter rulings to see if anything applies that can help you, Hintz says.

- **Document your payment carefully.** Make sure you call it restitution, compensation, or compensatory damages. "Proper and express characterization is important. It can make the difference of whether you get a deduction or not," Griffith says. The IRS may still challenge the deduction, but labeling helps. Failing to state exactly what the payment is for may cause you to prove the payment's intent as compensation, restitution or civil damages, and not a fine or penalty.

- **Enlist your accountant or tax attorney.** If you have any doubts, run the settlement or repayment and any possible deduction by your accountant or tax counsel to strategize, especially if the monetary amounts are substantial, Hintz says. If you have to, slow the settlement down to look at the tax impact, Hintz says.

- **Don't forget other tax rules that may affect your deduction.** For example, while you might theoretically be allowed to take an overpayment previously reported as income as a loss on your tax return, you may not be able to deduct all of it, because it's an itemized deduction, and subject to limitations based on the amount of income earned, Griffith notes.

IRS rulings comfort physicians

Many physicians don't realize some payments made to the government and payers are tax deductible and leave money on the table.

But private letter rulings, like an advisory opinion from HHS' Office of Inspector General (OIG), apply only to the individuals requesting them, and aren't as reliable as a court decision, says attorney Pat Hintz, with Quarles & Brady in Milwaukee, Wis.

"A private letter ruling does offer insight to how the IRS thinks," but can take the sting out of returning an overpayment, she adds.

It’s also acceptable to pursue the deduction if you believe you have a shot at it. “It’s okay to be aggressive on taxes so long as you have a reasonable basis. Usually at least you can come to a compromise with the IRS, so you’re still ahead [tax-wise],” Hintz says. “It’s a great opportunity in the appropriate case. Any provider has a lot of offsets and repayments.”