Short Form Order

SUPREME COURT - STATE OF NEW YORK
TRIAL TERM, PART 25 NASSAU COUNTY

PRESENT:

Honorable Karen V. Murphy
Justice of the Supreme Court

---x

ONE BEACON INSURANCE GROUP and any and all of Its subsidiaries and affiliates, including, but not limited to AUTOONE INSURANCE COMPANY, GENERAL ASSURANCE COMPANY,

Index No. 4055/06

Plaintiffs,

Motion Dated: 3/27/07
4/04/07
Motion Submitted: 5/11/07
Motion Sequence: 004, 005

-against-

MIDLAND MEDICAL CARE, P.C., NUCARE MEDICAL, P.C., ACUCARE ACUPUNCTURE, P.C., MOUNT SINAI DENTAL SURGERY, P.C., CPN CHIROPRACTIC, P.C., GILRAY D. BANAWIS, P.T., P.C., PDG PSYCHOLOGICAL, P.C., DELTA EXECUTIVE SERVICES, INC., HENRY VALEVICH, RITA KUCHEROVSKY URMAN, ALEX URMAN, DOUGLAS SPIEL, M.D., MATTHEW MILLER, M.D., PHILIP DAUBER GOLDSTEIN, PhD., DAVID GALVIN, D.D.S., VICTORIA ZAKHAROV, GILRAY D. BANAWIS, GUARDIAN MEDICAL CARE, P.C., CATALINA ANCA GRIGORESCU, PROSCAN IMAGING, P.C., RAPID MANAGEMENT, INC., DAVID STEMERMAN, M.D., CHARLES NGUYEN, WALTER (VLADIMIR) LIBES, SERGE GAYETSKY, EUGENE VINDERMAN,

Defendants.

---x

The following papers read on this motion:

Notice of Motion/Order to Show Cause.....XX
Answering Papers.....XX
Reply.....XX
Briefs: Plaintiff's/Petitioner's.....X
Defendant's/Respondent's.....X

Motion by defendants David Stemerman, M.D. and Proscan Imaging, P.C. for summary judgment dismissing the complaint is denied. Cross-motion by plaintiffs pursuant to CPLR § 3126 to strike defendants' answers for failure to comply with disclosure is granted to the extent that defendants shall provide discovery as directed below.

This is an action for a declaratory judgment that defendants are ineligible for no fault reimbursement because they are in violation of state licensing requirements. Plaintiffs also assert claims for fraud and unjust enrichment and seek to recover no fault benefits previously paid to defendants.

Plaintiff One Beacon Insurance, is a group of affiliated insurance companies. Plaintiffs AutoOne Insurance Company and General Assurance Company are insurers affiliated with One Beacon who issue policies of automobile insurance. Defendants Gilray Banawis, Douglas Spiel, Matthew Miller, Philip Goldstein, David Gavlin, and David Stemerman are health care providers who treat patients injured in automobile accidents. Defendants Midland Medical Care, Nucare Medical, Acucare Acupuncture, Mount Sinai Dental Surgery, CPN Chiropractic, PDG Psychological, Guardian Medical Care, and Procscan Imaging are the professional service corporations through which the health care providers practice. The patients assign their no fault claims to the professional corporations which then submit the claims to the insurance companies. The defendants Serge Gayetsky, Eugene Vinderman, Henry Valevich, Walter Libes, and Rita and Alex Urman, perform management services for the professional corporations, including preparing and submitting no fault claims. The defendants who perform these management services are not licensed to practice any health care profession.

Pursuant to Insurance Law § 5103, every automobile insurance policy must provide for payment of so-called "no fault," or "first party benefits," to occupants of the covered vehicle who sustain loss through the use or operation of the vehicle. Sec. 5102(b) of the Insurance Law defines "first party benefits" as payment to reimburse the injured person for

"basic economic loss", less certain deductions. The deductions include 20% of lost earnings, amounts recoverable under social security disability and workers compensation, and amounts deductible under the policy (***Insurance Law § 5102[b]***). Under Insurance Law § 5102(a), "basic economic loss" means necessary medical expenses and lost earnings up to $50,000.00. Thus, in accordance with the statutory scheme, expenses for necessary medical services, including x-rays and MRI's, are ordinarily reimbursable no fault benefits.

However, under the regulations of the Insurance Department, a provider of health care services is not eligible for reimbursement under § 5102(a) of the Insurance Law if the provider fails to meet any applicable New York State or local licensing requirement necessary to perform such service in New York or any other state in which such service is performed. (***11 NYCRR § 65-3.16 [a] [12]***).

If the health care provider is a professional service corporation, § 1507 of the Business Corporation Law requires that any individual who holds shares in the professional corporation be licensed to practice the profession. Business Corporation Law § 1507 in pertinent part provides, "A professional service corporation may issue shares only to individuals who are authorized by law to practice in this state a profession which such corporation is authorized to practice. . . ." Under Title VIII of the Education Law, a license is required to practice various health care professions including medicine, dentistry, psychology, and chiropractic. (See ***Education Law § 6500 et seq***). Section 1508 of the Business Corporation Law provides that no individual may be a director or officer of a professional service corporation unless the individual is licensed to practice the profession. If a professional service corporation is in violation of either of these licensing requirements, an insurer may deny the professional corporation reimbursement for no fault benefits. (***State Farm Mut. Auto. Ins. Co. v. Mallela***, 4 N.Y.3d 313, 320, 827 N.E.2d 758, 794 N.Y.S.2d 700 [2005]).

Defendant Dr. David Stemerman is a radiologist who practices through defendant Proscan Imaging, P.C. Plaintiffs allege that Proscan Imaging is ineligible for no fault reimbursement because it is "owned, operated, controlled, and managed" by defendants Serge Gayetsky, Eugene Vinderman, Henry Valevich, and Rita and Alex Urman, who are not licensed to practice medicine. Plaintiffs allege that these defendants own and control Proscan through defendant Rapid Management, Inc., which performs various administrative services for the professional corporation. Defendants Dr. David Stemerman and Proscan Imaging move for summary judgment on the ground that Dr. Stemerman, who is the sole shareholder of Proscan, is, as a matter of law, in control of the professional service corporation.

In ***State Farm Mut. Auto. Ins. Co. v. Mallela, supra,*** the Court of Appeals held that an insurer may withhold payment for medical services provided by "fraudulently incorporated" enterprises to which patients have assigned their no fault claims. In ***Mallela***, unlicensed individuals paid physicians to use their names on certificates of incorporation and other documents filed with the Department of State to establish medical service corporations (***Id.*** at 319). Once the medical service corporations were established under the cover of the nominal physician-owners, the non-physicians actually operated the companies (***Id***). The non-physicians caused the corporations to hire management companies owned by the non-physicians, which billed the medical corporations at inflated rates for routine services (***Id.*** at 319-20). Thus, the actual profits did not go to the nominal owners but were channeled to the non-physicians who owned the management companies.

In ***Mallela***, the patients received appropriate care from licensed health care professionals, and the insurer never claimed that the medical care was unnecessary or improper. The fraud was "in the corporate form rather than on the quality of care provided" (***Id.*** at 320). The court stated that mere failure to observe corporate formalities would not render the provider ineligible. However, willful and material failure to abide by state and local licensing requirements would be tantamount to fraud and render the provider ineligible for no fault reimbursement (***Id.*** at 322). In ***Mallella***, the Court of Appeals did not reach the issue of whether the insurer could recover claims previously paid based upon a theory of fraud or unjust enrichment (***Id.***). The Court did state, however, that "[N]o cause of action for fraud or unjust enrichment would lie for any payments made by the carriers before [the] regulation's effective date, i.e., April 4, 2002." (***Id.***)

The question of whether a fraudulently formed medical corporation was entitled to be reimbursed under the no fault law had been certified to the New York Court of Appeals by the United States Court of Appeals for the Second Circuit (***State Farm Mutual Automobile Insurance Co. v. Mallela***, 372 F.3d 500 [2d Cir., 2004]). In certifying this question, the U. S. Court of Appeals noted our state's longstanding concern that the "corporate practice of medicine" would create ethical conflicts and undermine the quality of care afforded to patients (***Id.*** at 503). Additionally, State Farm asserted that the corporate practice of medicine was associated with more traditional forms of fraud, such as billing for services not provided, billing for services that were medically unnecessary, and billing for services at the wrong rate (***Id.*** at 504, 507).

In answering the certified question, our Court of Appeals held that if a medical service

corporation is fraudulently, that is secretly, owned or controlled by an unlicensed individual, the medical service corporation is not entitled to be reimbursed for no fault benefits (***Mallella***, 4 N.Y.3d at 321.) A medical services corporation may be under the de facto control of an unlicensed individual even if that person is not a nominal shareholder, director, or officer of the professional corporation (***AIU Ins. Co. v. Deajess Medical Imaging***, 2/10/06 N.Y.L.J. P.22, Col. 1 [Sup. Ct. Nass. Co., 2/10/06]). In ***AIU Ins. Co. v. Deajess Medical Imaging***, ***supra***, Justice Bucaria held that to be in de facto control, the unlicensed individual must possess the functional equivalent of managerial authority and exert some influence over the medical services provided by the corporation. The performance of routine administrative tasks is not de facto control. However, if a lay person were to have financial control of the professional corporation, an inference would arise that the medical services provided by the corporation were effected.

On a motion for summary judgment, it is the proponent's burden to make a prima facie showing of entitlement to judgment as a matter of law, tendering sufficient evidence to demonstrate the absence of any material issues of fact (***JMD Holding Corp. v. Congress Fin. Corp.***, 4 N.Y.3d 373, 384, 828 N.E.2d 604, 795 N.Y.S.2d 502 [2005]). Failure to make such a prima facie showing requires denial of the motion, regardless of the sufficiency of the opposing papers (***Id***). However, if this showing is made, the burden shifts to the party opposing the summary judgment motion to produce evidentiary proof in admissible form sufficient to establish the existence of material issues of fact which require a trial (***Alvarez v. Prospect Hosp.***, 68 N.Y.2d 320, 324, 501 N.E.2d 572, 508 N.Y.S.2d 923 [1986]).

In support of their motion for summary judgment, defendants submit a deposition of Dr. Stemerman, which was taken in a series of actions to recover no fault benefits prosecuted by Proscan against State Farm in Civil Court, Queens County. At the deposition, Dr. Stemerman testified that he is the sole shareholder of Proscan and he performs or oversees all medical services provided by the professional corporation. Dr. Stemerman testified that he was the sole signatory on Proscan's bank account and authorized his own monthly draw from the corporation. Dr. Stemerman testified that he hired and fired all medical personnel and retained Proscan's accountants. The Court concludes that defendants have made a prima facie showing that Proscan is not controlled by any unlicensed individuals. Thus, the burden shifts to plaintiffs to offer proof that an unlicensed individual is in fact in control of Proscan.

In opposition to defendants' motion for summary judgment, plaintiffs also rely upon Dr. Stemerman's deposition, which was taken in the Civil Court actions. Explaining how Proscan was formed, Dr. Stemerman testified that, about five years after becoming a physician, he decided to be "a little bit more entrepreneurial." In January 2003, Dr. Stemerman entered into a "leasing, billing, and administrative services agreement" with

Premier Medical Management whereby Premier would provide the doctor with a "turn key" radiology facility. According to the agreement, Premier was to provide office space, medical equipment, supplies and administrative services. Proscan was to pay a monthly "leasing fee" for these services based on the total cost, plus an agreed upon percentage. For the first year of the agreement, the leasing fee was set at $156,000.00 per month based upon cost estimates for rent, equipment, and other charges and an agreed upon percentage of 5%. Although the leasing fee was to be "reconciled" after each quarter based upon actual costs, no adjustment based upon Premier's actual costs was ever made. The agreement between Proscan and Premier recites that it was not to "control, interfere with or inhibit any physician-patient relationships." This recital confirms that Dr. Stemerman recognized the danger that was inherent in the parties' arrangement. Nevertheless, the self-serving nature of the recital gives little assurance that Dr. Stemerman's fears were not realized. In any event, during 2003, Rapid Management took over the contract on the same terms under which Premier had operated.

In June 2006, Proscan entered into a new agreement with Rapid Management whereby Rapid would provide only billing and collection services for a set fee of $50,000.00 per month. Proscan assumed the office and equipment leases and began paying the lessors directly at that time. After the new system was implemented, it was soon discovered that Premier and Rapid had been charging Proscan $8,500.00 more per month than the actual rent and had also been overcharging for the equipment lease and maintenance services. Plaintiffs claim that the tax returns and other financial data indicate that during the period when Proscan was being actively managed by Premier and Rapid, the management companies were paid over 75% of Proscan's revenue.

The Court concludes that plaintiffs have come forward with sufficient evidence to create a triable issue as to whether Proscan was financially controlled by unlicensed individuals. The receipt by an unlicensed individual of a disproportionate share of the professional corporation's revenue is evidence that the unlicensed individual is in de facto ownership or control of the professional corporation (***AIU Ins. Co. v. Deajess Medical Imaging, supra.***, see also ***Education Law § 6509-a*** [prohibiting fee splitting between physician and lay person]). The charging of excessive leasing and equipment fees gives rise to the inference that unlicensed individuals were able to appropriate Proscan's profit because they were in de facto control of the professional corporation. As noted above, the evidence of improper financial control gives rise to an inference that the quality of medical care may have been also effected.

It appears that Proscan attempted to regain control over its medical practice when the new arrangement with Rapid Management was negotiated. However, even though

administrative services are now limited to billing, the management company may yet be receiving excessive compensation. As Justice Bucaria noted in ***Deajess***, the charging of a reasonable processing fee for preparation of no fault claims would not of itself mean that revenue was being shared in an improper manner. Nevertheless, based upon the documents submitted, a trial is necessary to determine whether Rapid continues to receive a disproportionate share of the revenue of Proscan. Because there is a triable issue as to whether Proscan is under the de facto control of unlicensed individuals, defendants' motion for summary judgment as to plaintiffs' claim for declaratory relief is denied.

The Court notes that defendants have failed to submit an affirmation from Dr. Stemerman to the effect that all of the procedures for which claims were submitted were medically necessary and were in fact performed. Thus, defendants have failed to make a prima facie showing that they are entitled to judgment as to plaintiffs' claims for fraud and unjust enrichment. Defendants' motion for summary judgment dismissing plaintiffs' claims for recovery of no fault benefits previously paid is also denied.

Plaintiffs have requested numerous documents, which are relevant to the issue of whether Proscan is owned or controlled by unlicensed individuals. Accordingly, plaintiffs' motion to strike defendants' answers is granted only to the extent that within 30 days of service of a copy of this order defendants shall produce the following:

1) all documents reflecting Premier and Rapid's actual costs for items covered by the agreements with Proscan, including without limitation rent, equipment, supplies, and payroll costs.

2) copies of all cancelled checks (front and back) reflecting payments made by Proscan to any of the named defendants or to Premier Medical Management for the period January 2003 to present.

3) all financial statements prepared by or on behalf of Proscan.

4) all IRS form W-2's and 1099's issued by Proscan, including those issued to Dr. Stemerman, from January 2003 to date.

5) Proscan's bank statements for the years 2003 to date. While bank records are ordinarily confidential, a sufficient showing of need for the bank statements has been made. ***CPLR § 3101(a)*** requires the full disclosure of all information that is material and necessary to the defense or prosecution of an action. The "material and necessary" requirement

mandated by ***CPLR § 3101(a)*** is to be liberally construed to require disclosure where the matter sought will assist in trial preparation by sharpening the issues. (***U.S. Ice Cream Corp. v. Carvel Corporation***, 190 A.D.2d 788, 593 N.Y.S.2d 861 [2d Dept., 1993]).

Plaintiffs' motion to strike the answers and for other relief is otherwise denied.

The foregoing constitutes the Order of this Court.

Dated: July 20, 2007
Mineola, N. Y.

Karen V. Murphy
J. S. C.