

OFFICIAL TRANSCRIPT
PROCEEDINGS BEFORE
THE SUPREME COURT
OF THE
UNITED STATES

CAPTION: DONNA E. SHALALA, SECRETARY OF HEALTH &
HUMAN SERVICES, Petitioner v. GUERNSEY
MEMORIAL HOSPITAL

CASE NO: No. 93-1251

PLACE: Washington, D.C.

DATE: Monday, October 31, 1994

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1 IN THE SUPREME COURT OF THE UNITED STATES
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3 DONNA E. SHALALA, SECRETARY OF :
4 HEALTH & HUMAN SERVICES :
5 Petitioner :
6 v. : No. 93-1251
7 GUERNSEY MEMORIAL HOSPITAL :
8 - - - - -X
9 Washington, D.C.
10 Monday, October 31, 1994
11 The above-entitled matter came on for oral
12 argument before the Supreme Court of the United States at
13 11:05 a.m.
14 APPEARANCES:
15 KENT L. JONES, ESQ., Assistant to the Solicitor General,
16 Department of Justice, Washington, D.C.; on behalf of
17 the Petitioner.
18 SCOTT W. TAEBEL, ESQ., Columbus, Ohio; on behalf of the
19 Respondent.
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1 PROCEEDINGS

2 (11:03 a.m.)

3 CHIEF JUSTICE REHNQUIST: We'll hear argument
4 next in Number 93-1251, Donna Shalala v. Guernsey Memorial
5 Hospital. We'll hear from you, Mr. Jones.

6 ORAL ARGUMENT OF KENT L. JONES

7 ON BEHALF OF THE PETITIONER

8 MR. JONES: Mr. Chief Justice and may it please
9 the Court:

10 Under the Medicare Act and section 413.9 of its
11 implementing regulations, the United States reimburses the
12 reasonable cost of services provided to Medicare
13 beneficiaries. The Secretary of HHS makes the
14 reimbursement determinations under the act subject to
15 judicial review under the APA.

16 This case concerns whether, in making these
17 determinations, the Secretary is required by her
18 regulations to apply generally accepted accounting
19 principles even when she rationally determines in a
20 particular case that application of those principles will
21 not arrive at the reasonable cost for the services
22 provided during the reimbursement period.

23 In our view, the language of the regulations
24 contains no such requirement. Section 413.20 of the
25 regulations, on which the court of appeals relied,

1 specifies that providers are to maintain their cost
2 records by use of standardized definitions and accounting
3 procedures and practices, and states, and I quote, "that
4 essentially reimbursement under the act involves making
5 use of that cost data to arrive at equitable and proper
6 payment" while nothing in these general admonitions about
7 maintaining and using cost data to arrive at equitable and
8 proper payment represents a clear, unambiguous and firm
9 undertaking by the Secretary that she will always apply
10 GAAP in reimbursement determinations.

11 QUESTION: Well, Mr. Jones, you say that this
12 regulation, 413.20, just governs how Medicare providers
13 are to report their costs to the HHS --

14 MR. JONES: To maintain their costs.

15 QUESTION: -- or to the intermediary, and if
16 that's so, then what regulations say how HHS will
17 determine the method to be used in providing
18 reimbursement?

19 MR. JONES: Section 413.9 of the regulation is
20 the substantive standard that provides that all payments
21 will be made with respect to reasonable costs. That's the
22 substantive standard. Section 413.20 --

23 QUESTION: Well, if you mandate the provider to
24 follow generally accepted accounting principles, and I
25 guess you concede that under generally accepted accounting

1 principles these amounts would be reportable and
2 recoverable up front --

3 MR. JONES: No, we --

4 QUESTION: -- then I don't know why the
5 Secretary shouldn't follow the same program in determining
6 what's reimbursable.

7 MR. JONES: I think the easiest way for me to
8 explain that is to point out that, even if a provider
9 follows a particular format in submitting the costs, that
10 does not mean that the costs thus submitted are reasonable
11 costs to be reimbursed under Medicare.

12 For example, under accrual accounting, which is
13 what the regulation talks about, or even under GAAP, a
14 hospital with gold plumbing could arrive at a valid
15 accounting statement for its actual depreciation costs.

16 QUESTION: Well, but now wait a minute, I
17 thought the Secretary had said, yes, the costs we're
18 talking about here in this case are reimbursable, we're
19 just going to do it annually, we're not going to do it up
20 front. Don't we assume that these are reasonable
21 reimbursable costs?

22 MR. JONES: Well, as the administrator pointed
23 out in this case, the timing, the coordination of the
24 timing of the cost with the periods benefited by that cost
25 is as important in the determination of reasonable cost as

1 the amount of the cost.

2 QUESTION: Well, but this isn't gold-plated
3 plumbing. This is something that the Secretary says, yes,
4 we'll let you have, but we're going to do it annually.
5 Isn't that right?

6 MR. JONES: Well, there's -- there are several
7 points involved in your question, and let me see if I can
8 address them.

9 The first point is whether these regs require
10 that we imply -- employ GAAP, and our point is, the text
11 of the regulations doesn't require it, and it would be
12 illogical for any such requirement to exist, because GAAP
13 has only a remote relationship to whether costs are
14 reasonable.

15 QUESTION: Mr. Jones, if you could give an
16 answer to Justice O'Connor's question, did the reporter
17 report accurately, that would be helpful. I think it was
18 clear up until your brief in this case that you conceded
19 that the hospital's report form was okay. It was a proper
20 report. I couldn't tell for sure whether you were
21 continuing to make that concession in your brief here.
22 Did the hospital report properly?

23 MR. JONES: The hospital reported its expenses
24 in a proper amount, and by interpretation of the agency's
25 regulations, what the hospital is required to do is to

1 apply the accrual basis of accounting, and it applied an
2 accrual basis of accounting. The question is, having met
3 the format requirement of the reimbursement requirement,
4 whether the costs thus reported are reasonable with
5 respect to the services provided during the --

6 QUESTION: Just -- did the hospital report
7 properly? You seem to be saying, the reimbursement
8 doesn't have to match the report, but the hospital asked
9 the question, we have to fill out this form and claim our
10 costs. Was that cost report proper in compliance with the
11 statute and regulations?

12 MR. JONES: It was proper as to amount and not
13 as to the timing of the attribution of the costs to the
14 periods benefited by the expense.

15 QUESTION: So it was an improper cost report.
16 You're not making the argument that, yes, the report was
17 proper, but the reimbursement doesn't have to correspond
18 to the report?

19 MR. JONES: Well, that is -- maybe I'm
20 misunderstanding your question about what is a cost
21 report.

22 QUESTION: What the hospital filed, should the
23 hospital, instead of taking this all at once have split it
24 up, have amortized it, as you did in your reimbursement?

25 MR. JONES: Yes. If they had followed PRM 233,

1 that is the way they would have submitted their cost
2 report. It makes little sense for the Secretary to
3 require its intermediaries to recast these expenses when
4 they're submitted in a manner that doesn't correspond to
5 the Secretary's reimbursement rules.

6 QUESTION: But if they follow generally accepted
7 accounting principles, they could have filed it exactly as
8 they did.

9 MR. JONES: They did follow, and did file --

10 QUESTION: They did do that, didn't they?

11 MR. JONES: -- based upon generally accepted
12 accounting principles for this type of transaction.

13 QUESTION: And in theory, the regulation 413.20
14 says if you do that you're -- that's proper for your
15 report.

16 QUESTION: I don't know what 413.20 means, if it
17 doesn't mean that. It seems to me you have to concede
18 that the report filed was proper, or else 413.20 has no
19 meaning.

20 MR. JONES: I will concede it for purposes of
21 this argument, that we don't have a problem with providers
22 estimating their costs in an accurate manner, which they
23 did, and submitting them to us for us to make a
24 determination of what reasonable cost is.

25 QUESTION: Not don't have a problem, you've told

1 them to do that in 413.20.

2 MR. JONES: Well, I don't want to quibble, but
3 on the other hand, this is our regulation, and we're
4 entitled to interpret it, and all that that regulation --

5 QUESTION: No, but there's -- may I just raise
6 this basic question about your interpretation? As I
7 understand you, you're saying 413.9 is the operative
8 regulation on reimbursement, 413.20 and 413.24 are simply
9 accounting and reporting regulations, and accounting does
10 not necessarily determine reimbursability.

11 MR. JONES: Yes.

12 QUESTION: Isn't it very odd, should we not
13 consider it very odd in trying to make sense of 413.20 and
14 413.24 that the only regulation on reimbursement is at
15 this very high level of generality, 413.9, whereas all of
16 the detailed regulations, or regulations of comparatively
17 greater detail, do not even address the ultimate issue of
18 reimbursability. That seems to me an unreasonable way for
19 us to read, and, with respect, for you to read, 413.20 and
20 413.24.

21 MR. JONES: It is easy to gloss over the
22 specific words of these regs, and I certainly don't want
23 to do that, but I think that it's also important to
24 realize that the statute and the reg 413.9 are the
25 substantive standard. Congress adopted reasonable cost as

1 the substantive standard. We couldn't alter that standard
2 if we wanted to, and we don't want to.

3 QUESTION: Well, true, but in trying to make
4 sense of 20 and 24, there's something very strange about
5 your going to the trouble of greater detail in those, when
6 you never go to the trouble, or the Secretary never goes
7 to the trouble, on your reading, of addressing in detail
8 the question of reimbursability.

9 MR. JONES: Well, the only detail referred to in
10 413.20 is advice that you should use standard definitions
11 in accounting practices.

12 QUESTION: Which is the detail upon which this
13 case turns.

14 MR. JONES: No, the detail on which this case
15 turns is --

16 QUESTION: I mean, it's a pretty important
17 detail.

18 MR. JONES: -- is whether these costs are --

19 QUESTION: If generally accepted accounting
20 principles drives reimbursability, the case is going to go
21 one way, and if it doesn't, it's going to go the other
22 way.

23 MR. JONES: The detail that should answer this
24 case is whether these are reasonable costs. All that the
25 regs that have been relied on by the courts below refer to

1 is how you are to prepare and maintain and submit your
2 cost data.

3 QUESTION: I realize that, but what about the
4 oddity of addressing accounting in so much greater detail
5 than addressing reimbursability? Is that in fact a
6 reasonable way for us to read 20 and 24?

7 MR. JONES: I don't see all of the detail in
8 413.20 and 24 that you're referring to. Let me explain --

9 QUESTION: Well, there is the detail of
10 reference, in effect, to generally accepted accounting
11 principles.

12 MR. JONES: Not by words, and not by
13 interpretation.

14 QUESTION: Not by words, but you concede that in
15 fact it is picked up by the words that are used, do you
16 not?

17 MR. JONES: No, I don't concede that, Justice
18 Souter. The statute -- the reg 413.24 refers to
19 submitting your cost data on the accrual basis of
20 accounting. It defines that term in the reg simply in a
21 manner that differentiates that from cash basis
22 accounting.

23 QUESTION: Yes.

24 MR. JONES: Now, the decisions of the Accounts
25 Principles Board are quite clear that GAAP is just a

1 subset and not an exhaustive list of all accrual
2 accounting methodologies, and it's with that thought in
3 mind that I think the Court should consider the consistent
4 interpretation of the Secretary since these regs were
5 adopted over 20 years ago. Her --

6 QUESTION: Let me -- if I may, let me just go to
7 20, leaving aside the specific reference, what was it, in
8 24 on accrual basis -- does 20 pick up generally accepted
9 accounting principles?

10 MR. JONES: I don't see it in the text, and more
11 importantly --

12 QUESTION: It doesn't use that phrase --

13 MR. JONES: It certainly --

14 QUESTION: -- but it refers to --

15 MR. JONES: It says standard accounting
16 practices.

17 QUESTION: -- standards of national
18 organizations, and it refers to -- I believe it refers, in
19 effect, to insurance organizations.

20 MR. JONES: No. Actually, you're -- that's the
21 statute. The statute makes a reference to --

22 QUESTION: I'm sorry. I'm sorry.

23 MR. JONES: -- considering, among other things,
24 the reimbursement criteria of national organizations. The
25 reg that you're talking about just says, maintain your

1 cost data so we can audit it, and we want you to maintain
2 it by reference to standard definitions and accounting
3 practices, and then the last sentence explains the context
4 that I'm trying to inarticulately establish, and that's,
5 last sentence says, essentially reimbursement under the
6 act involves making use of this data to arrive at
7 equitable and proper payment.

8 Now, I understand essentially means mainly
9 involve, making use of means we're going to do something
10 to the data that you've given us to arrive at something
11 else, and that something else is equitable and proper
12 payment, and to know what that means we go to the statute
13 and 413.9, which says reasonable cost.

14 QUESTION: I understand, Mr. Jones. However,
15 the statute requires that the manner of determining
16 reimbursement be prescribed by regulations. Is it your
17 contention that the only regulation the Secretary has
18 issued to comply with that statutory mandate is 413.9?
19 That's it?

20 I mean, Congress goes to the trouble to say, you
21 know, the reasonable costs shall be actually incurred, and
22 shall be determined in accordance with regulations
23 establishing the method or methods to be used.

24 MR. JONES: That's what it says.

25 QUESTION: Congress does not always require

1 regulations to be issued. Here, it specifically does, and
2 you tell us that the only thing the Secretary did to
3 comply with that was 14.9, which is what, you
4 know -- almost nothing.

5 MR. JONES: Justice Scalia, the statute doesn't
6 say the Secretary shall issue regs, it says, reasonable
7 costs shall be determined in accordance with the regs.
8 These reasonable cost cases --

9 QUESTION: Not the regs. In accordance with
10 regulations --

11 MR. JONES: -- regulations adopted by the
12 Secretary.

13 QUESTION: You don't think that's a requirement
14 to issue regulations?

15 MR. JONES: I think that for the last 20-some
16 years the Secretary, as in this case, has been making
17 determinations as to reimbursable costs under section
18 413.9, which is the requirement that payment shall be made
19 of reasonable costs.

20 QUESTION: Are there other indications, other
21 illustrations, apart from this one, where the report from
22 the hospital is correct, it's a proper report, it reports
23 the cost --

24 MR. JONES: Yes.

25 QUESTION: -- which is reasonable, a reasonable

1 cost, so the debate is, as here, not whether you can take
2 this cost, but when?

3 MR. JONES: Yes. Yes, there's a very good
4 example that I'd like to describe in some detail for you.
5 It came out of the Research Medical Center case in the
6 Eighth Circuit, and what the court held -- what that was
7 about was where, in preconstruction of a facility,
8 interest was accruing on a debt. It was reasonable
9 interest. It was reasonably related to the construction
10 of this facility.

11 What the Secretary determined in a PRM was that
12 this type of preconstruction interest should not be paid
13 by Medicare, it should be capitalized until the building
14 is finished, and then it should be reimbursed over an
15 amortized period while the building's being used.

16 Now, the reason that she did it that way was
17 because it is extremely important in Medicare to align the
18 costs incurred over the periods benefited by this cost,
19 precisely because the hospital's level of reimbursement,
20 the percentage of its costs that are repaid, fluctuates
21 depending upon the level of service.

22 And in the Research Medical Center case, the
23 court gave the example of a cost incurred by a hospital in
24 year 1 that provides benefits for 10 years, and the court
25 said that if the Medicare payment, if Medicare paid that

1 whole cost in year 1, and then the hospital stopped
2 covering Medicare patients in years 2 and thereafter, the
3 result would be Medicare fully paid for costs that
4 benefited non-Medicare patients in other years. That
5 result would precisely contradict the statutory cross-
6 subsidization rule, which is that Medicare funds shall not
7 be used to provide benefits for non-Medicare patients.

8 QUESTION: That depends on whether you regard
9 these charges as charges that are attributable to what was
10 done in the past, or, rather, as charges that are
11 attributable to the new financing, which is really a very
12 theological question.

13 MR. JONES: It --

14 QUESTION: And I, you know, I don't know, you
15 could answer it either way, and generally accepted
16 accounting principles have answered it the other way.

17 Now, if you had wanted to answer it your way and
18 had put that answer down in regulations instead of in what
19 you call the Secretary's Provider Reimbursement Manual, we
20 would have a lot more information in front of us from that
21 regulation which might have been challenged in court at
22 the time it was issued, but you didn't do that. You just
23 put it in your manual.

24 MR. JONES: No one has doubted that this
25 particular application of the amortization principle in

1 this case is a rational application. What you seem to be
2 referring to, Justice Scalia, is the question of whether
3 the only way the Secretary could adopt a reasonable
4 rule --

5 QUESTION: In fact, it not only is rational,
6 it's the one that GAAP itself used up until 1972, isn't
7 it?

8 MR. JONES: And when GAAP adopted a different
9 rule, 4 of the 18 members of the board didn't like it --

10 QUESTION: Do I understand you correctly --

11 MR. JONES: -- said, let's stay with the old
12 method.

13 QUESTION: -- that there's no debate between the
14 two sides that this is a reasonable choice for her to
15 make, and she could have made it in a regulation, the only
16 question is, must she do it in the regulation and not
17 stick it in the PRM?

18 MR. JONES: Right. And there's two aspects to
19 that question. The first is whether she has to do it in a
20 regulation because her regs require GAAP, which I don't
21 think they do. They don't plausibly do that by their
22 terms, or by interpretation.

23 The only other way that she could be required to
24 adopt this by regulation would be if some statute
25 compelled that requirement. The only statute is the one

1 Justice Scalia -- that's applicable is the one Justice
2 Scalia referred to, which says reimbursement shall be
3 determined in accordance with the regs establishing
4 methods.

5 She has such regs. The question is whether she
6 has to adopt every detailed subconcept as a regulation,
7 and this Court has never held any agency to that
8 requirement. The SEC --

9 QUESTION: Mr. Jones, can I ask you a question
10 about exactly what regulation is being interpreted --

11 MR. JONES: Yes, sir.

12 QUESTION: -- in the interpretive bulletin? I
13 think you rely primarily on the general 413.9. Is it not
14 arguable that that was really an interpretation of the
15 interest expense regulation, because that's where it
16 appears in the manual?

17 MR. JONES: This is a form of interest expense
18 issue, but most of the other subregs refer to -- for
19 example, in the capital expense area -- say reimbursement
20 is limited to the following types of costs, and then talk
21 about those costs, types of capital costs, but the
22 substantive ceiling on these types of capital costs is in
23 413.9, which is the reasonable cost limit.

24 QUESTION: You do not contend that this bulletin
25 is an interpretation of 413.153?

1 MR. JONES: I think it's an -- I think the
2 administrator was quite clear that it was an
3 interpretation of 413.9, and we agree with that.
4 Moreover, I would direct the Court --

5 QUESTION: But it falls in the interest expense
6 portion of the manual. That's what puzzles me.

7 MR. JONES: Well, I suppose every reasonable
8 expense would be probably an expense -- I'm not sure. My
9 guess is that every type of expense is addressed somewhere
10 in the manual, but all of those descriptive provisions --
11 I mean, in the regulations, but all of those other
12 descriptive provisions are subject to 413.9, which is what
13 the administrator relied on here.

14 QUESTION: Are there any other regulations --
15 I'm not -- maybe I asked this before, but I'm not sure I
16 got a clear answer. The statute says that costs shall be
17 determined in accordance with regulations establishing the
18 method or methods to be used and the items to be included,
19 and the only regulation the Secretary has issued to which
20 that could possibly apply is 413.9. That's --

21 MR. JONES: No, I -- if I said that, I didn't
22 mean that. What I mean is --

23 QUESTION: What else is there?

24 MR. JONES: Okay, exactly what Justice Stevens
25 was talking about. There are other provisions, including

1 the accounting provisions --

2 QUESTION: In regulations?

3 MR. JONES: Yes, in regulations, that set out
4 the methods by which costs should be submitted, the types
5 of --

6 QUESTION: Not submitted. I'm not talking about
7 submission. I understand 413.20 deals with submission.
8 I'm talking about how costs are to be determined.

9 MR. JONES: Costs -- again, as Justice Stevens
10 referred to, 42 C.F.R. 413.153 sets out limits on the
11 capital, the types of capital costs that may be
12 reimbursed, but the bottom line substantive answer to your
13 question that the Secretary has relied on for over 20
14 years is that her authority is by statute and regulation
15 to make determinations of reasonable costs, and that that
16 is the manner in which these determinations are made.

17 Now, under NLRB v. Bell Aerospace, this Court
18 has acknowledged that it's up to the agency to decide
19 whether to proceed by adjudication or by regulation, and
20 in this case the --

21 QUESTION: Bell Aerospace did not involve a
22 statute that requires the Secretary to act by regulation,
23 or the -- I guess it was laid on an agency.

24 MR. JONES: I don't think this statute requires
25 the agency to act by regulation. It says, reasonable

1 costs shall be determined in accordance with regulations.
2 It doesn't say that every minute substandard as to what's
3 a reasonable cost must be set forth in a substantive rule.

4 QUESTION: Mr. Jones, you reported in your brief
5 that in fact, before you put this in the PRM, there was
6 extensive consultation, prior consultation. If you were
7 engaging in that, why didn't you just have it done by
8 notice and comment rulemaking?

9 MR. JONES: Of course, I haven't talked to those
10 people, and so I would be hypothesizing, but I can tell
11 you from representing Government agencies there's always a
12 tension, if not a risk, involved in making a concrete,
13 substantive rule that's binding that reduces the
14 flexibility.

15 You come up with the rule that you say, if A, B,
16 and C happen, then you won't get reimbursement, and the
17 hospitals then say, well, A and B happened, but we did D
18 instead of C. I'm not saying that -- what I'm trying to
19 say is, it's somewhat like in this Court sometimes when
20 you want to see an issue percolate in the court of appeals
21 some more before you adopt a substantive decision. The
22 agency wants to retain its flexibility before it makes
23 sure, and sometimes it does when it, after sufficient
24 experience, issues substantive rules.

25 What the agency -- the cost the agency pays for

1 not issuing the substantive rule is that it has to do what
2 it did in this case. It has to defend its determination
3 on the facts. It has to show that it wasn't arbitrary or
4 capricious.

5 QUESTION: Well, is your case weaker or stronger
6 without the manual?

7 MR. JONES: I don't think our case depends on
8 the manual. I think what the man -- what -- the relevance
9 of the manual to this case is, it shows that the hospital
10 had advance notice, it shows that we're behaving in a
11 consistent fashion, and it provides some additional
12 credibility to the administrator's finding, but it's the
13 administrator's findings that the Court needs to look to
14 to decide whether this is arbitrary or capricious.

15 QUESTION: Mr. Jones, I hate to keep coming back
16 to this, but I really consider it central to the case, and
17 I am frankly quite surprised the Government takes the
18 position that the Secretary has no obligation to act in
19 this field by regulation. What --

20 MR. JONES: No, it's --

21 QUESTION: How does one describe --

22 MR. JONES: It's --

23 QUESTION: -- the requirement that such
24 regulations may provide for a determination of the costs
25 of services on a per diem, per unit, per capita, or other

1 basis?

2 MR. JONES: I'm not suggesting --

3 QUESTION: You're saying that those regulations
4 which may or may not be issued, if they are issued have to
5 provide for that, but if they're not issued it doesn't
6 make any difference.

7 MR. JONES: Justice Scalia, I don't mean to
8 suggest that we don't have to issue regulations. We have
9 issued regulations. That's really not the question that
10 you have to consider. The question is whether, in
11 articulating substantive standards under the reasonable
12 cost statutory and regulatory threshold, we have to issue
13 minute subregulations in as detailed an issue as this one,
14 advance refunding on indebtedness.

15 I mean, the Provider Reimbursement Manual is
16 several inches thick. These -- this is not --

17 QUESTION: I would think it's a reasonable
18 position, however, that if you intend to depart from those
19 general practices and principles generally applied by
20 national organizations which are referred to in the
21 statute, at least those departures would be expected to be
22 by regulation.

23 MR. JONES: Well, there's no sub -- unless you
24 interpret the substantive regulation in a way that
25 requires GAAP to be applied, whether it results in

1 reasonable costs or not, whether it results in reasonable
2 timing or not, and unless you're willing to ignore the
3 consistent interpretation of the Secretary for 20 years to
4 the contrary, that question isn't presented.

5 Under this Court's decision as recently as last
6 year in Thomas Jefferson University, the Secretary's
7 consistent, rational, and contemporaneous interpretation
8 of her regulations is entitled to controlling weight, and
9 since both the court of appeals and the district court
10 agreed that it was not arbitrary or capricious to require
11 amortization in this context, and because the regs don't,
12 by their terms, require an unthinking application of GAAP
13 in every situation, under the APA the Court's -- I'm
14 sorry, the Secretary's decision should be affirmed.

15 QUESTION: Can I ask you, what is special about
16 this reg? That is, what is special about 232?

17 That is, if I read the thing to say, okay,
18 normally apply GAAP, not always, we have some discretion
19 there. Well, okay, going along with you that far, what's
20 special about this one? I mean, if in fact --

21 MR. JONES: Yes.

22 QUESTION: -- they bought all their medicine in
23 this year and wrote -- and didn't write the check till
24 next year, they'd accrue the expense this year.

25 MR. JONES: I --

1 QUESTION: So what's different about setting up
2 a trust fund which is irrevocable to pay back the premiums
3 on the --

4 MR. JONES: What's different is that what they
5 did was, in this kind of transaction the logic is very
6 simple. You incur some costs today to save more costs
7 tomorrow.

8 QUESTION: Right.

9 MR. JONES: You -- the Secretary has reasonably
10 concluded that it more accurately coordinates the extended
11 benefit of this transaction with the costs incurred to
12 affect it to amortize those costs --

13 QUESTION: Maybe it doesn't do that.

14 MR. JONES: -- over a future period.

15 QUESTION: I take it the reg is, reading it
16 back, that you pay it back amortizing it over the
17 difference between the time that you issue the refunding
18 bonds and the time that the holders of the refunded bonds
19 get their principal back, which could be next year, it
20 could be next month. It bears no particular relationship
21 to the period of time over which the interest will be
22 payable on the refunding bond --

23 MR. JONES: It does in this --

24 QUESTION: -- so it doesn't correlate with the
25 medical costs.

1 MR. JONES: My first point is -- and time's
2 running short -- that simply all you have to decide is
3 whether there's a rational basis for the Secretary to have
4 had a different view, and both the courts below agreed
5 that there was.

6 More importantly, in my view, these interest
7 costs of these bonds that are going to be extinguished
8 continue to accrue as an economic fact until they are in
9 fact extinguished, which in this case doesn't happen for
10 7 years, and so what the Secretary -- I'm sorry, what the
11 hospital has attempted to do is prepay the economic costs
12 of the old bonds, even though they remain in existence,
13 and what the Secretary has concluded is that amortizing
14 those prepayments over the remaining periods more
15 accurately coordinates the real benefits of this
16 transaction with the costs incurred.

17 I'd like to save my remaining time for rebuttal,
18 if I may.

19 QUESTION: Very well, Mr. Jones.

20 Mr. Taebel, we'll hear from you.

21 ORAL ARGUMENT OF SCOTT W. TAEBEL

22 ON BEHALF OF THE RESPONDENT

23 MR. TAEBEL: Thank you, Mr. Chief Justice, and
24 may it please the Court:

25 The issue in this case is one of timing. That

1 is, under the plain language of the general Medicare
2 reimbursement regulations, the Secretary can put off
3 payment for this admittedly reimbursable loss. Eight
4 Federal courts, including two circuits, have addressed
5 this precise question, and they have all answered it in
6 the negative. If the Secretary wants to amend or
7 supplement her existing reimbursement regulations, she
8 must do so through the promulgation of another regulation.

9 QUESTION: Well, Mr. Taebel, what would have
10 happened if the Secretary had issued no regulations
11 whatever pursuant to the statutory section we're talking
12 about here?

13 MR. TAEBEL: I believe, Mr. Chief Justice, as
14 Justice Scalia was indicating, the Secretary has an
15 obligation under the statute to promulgate her methods of
16 reimbursement.

17 QUESTION: Yes, but my hypothesis was, she
18 didn't do that.

19 MR. TAEBEL: If she did not do that, Your Honor,
20 and she initially determined that these costs should be
21 amortized, then perhaps she could do that. However, in
22 this case we have a sharp contrast between her positions
23 taken with respect to advance for funding losses.

24 QUESTION: So you say that she would have been
25 better off if she had issued no regulation under the

1 statute than if she'd issued the one she did?

2 MR. TAEBEL: No, Your Honor. She has already
3 issued a regulation. She's issued a regulation calling
4 for the GAAP approach.

5 QUESTION: Now, which regulation is that?

6 MR. TAEBEL: That is regulation, it's currently
7 codified at section 413.20, and it indicates, Your
8 Honor --

9 QUESTION: That doesn't call for the GAAP
10 approach, I didn't think, when I read it. It -- certainly
11 not in terms --

12 MR. TAEBEL: With due respect, Mr. Chief
13 Justice, that's all it can call for. There can be no more
14 standardized accounting practices widely accepted in the
15 hospital and related fields than GAAP. In fact, we count
16 seven times in the Government's appellee's brief before
17 the Sixth Circuit where they agreed that that statute
18 referred to GAAP. There is no issue with respect to that.

19 Under GAAP, if a cost was --

20 QUESTION: The statute or the regulation?

21 MR. TAEBEL: I'm sorry, Your Honor, the --

22 QUESTION: The statute or the regulation?

23 MR. TAEBEL: The regulation.

24 QUESTION: The regulation --

25 MR. TAEBEL: Yes.

1 QUESTION: -- referred to GAAP.

2 MR. TAEBEL: Yes. I'm sorry.

3 QUESTION: Standardized definitions, accounting
4 statistics, and reporting practices that are widely
5 accepted in the hospital and related fields are followed.
6 You say that requires GAAP?

7 MR. TAEBEL: Yes, Your Honor, because GAAP by
8 definition is the most standardized accounting practice,
9 widely accepted, that there is. There really is no issue
10 with respect to that, or there had not been until the
11 briefs before this Court.

12 QUESTION: Mr. Taebel, can I ask you kind of a
13 basic question that's running through my mind in this
14 case? As I understand your basic position, it is that
15 this issue is of sufficient importance that it ought to be
16 addressed by regulation following notice and comment.

17 MR. TAEBEL: That is correct, Your Honor.

18 QUESTION: Then how is it that if, when, prior
19 to 1972, GAAP had a rule that was consistent with the
20 Secretary's present rule, then GAAP changed its rule,
21 there was no notice and comment, but the effect of that
22 under your view is, that changed the rule?

23 MR. TAEBEL: Your Honor, there was no GAAP
24 pronouncement prior to 1972. That's exactly why APB
25 Opinion Number 26 came out to clarify different treatments

1 of this particular type of cost.

2 QUESTION: Let's assume it was clear under GAAP
3 it was permissible before, because there's no suggestion
4 that before 1972 it would have violated GAAP to follow
5 this procedure. That's correct, isn't it?

6 MR. TAEBEL: Yes.

7 QUESTION: All right, so assume this had been
8 spelled out in a GAAP ruling that was in existence from
9 1966 to 1972. Is it your position that GAAP, without any
10 public notice or comment, could in effect change the
11 regulation?

12 MR. TAEBEL: Your Honor, the regulation does not
13 refer to GAAP as it existed in 1966.

14 QUESTION: Well, but from '66 to '72, it
15 certainly fell into the language of the regulation as well
16 as it does since 1972.

17 MR. TAEBEL: That is true, Your Honor. However,
18 this has been the law, as it were, for the accounting
19 profession since 1972. If the Secretary wants to change
20 her general --

21 QUESTION: No, no. My question is, assume the
22 law in the accounting profession was just as clear before
23 '72 with the other rule as it has been since '72 with the
24 rule they have now. Could GAAP have changed the effect of
25 the Secretary's regulation by simply changing its rule

1 without notice and comment?

2 MR. TAEBEL: No, Your Honor, we are not claiming
3 that GAAP can turn an otherwise unallowable cost into a
4 cost related to patient care. That is not the --

5 QUESTION: No, but doesn't that beg the
6 question? I thought you were reading section 20 --
7 419.20, and I thought you were also reading the statute in
8 such a way that the appropriate phrases there simply pick
9 up whatever the generally accepted accounting principles
10 are at the time and incorporate them, so that if those
11 principles do in fact change, if a new bulletin is issued,
12 then the statute and the regulation would incorporate the
13 change. I thought that was -- that is not your position?

14 MR. TAEBEL: That is our position, Your Honor.

15 QUESTION: Well, but --

16 QUESTION: That's what I thought it was, too,
17 and I thought --

18 QUESTION: Why did you answer Justice Stevens
19 the way you did?

20 MR. TAEBEL: Well, because I believe Justice
21 Stevens was referring to the GAAP pronouncement prior to
22 1972, and there had been no official --

23 QUESTION: Now, but he gave you a hypothesis in
24 which he assumed that there was a position which then
25 changed. I assumed that your answer to Justice Stevens

1 would be that that would be no change in the Department's
2 policy at all, since the Department's policy is to follow
3 GAAP, whatever that is.

4 MR. TAEBEL: That's correct, Your Honor.

5 QUESTION: And therefore the amendment of GAAP
6 would not change the Department's policy. It continues to
7 be, to follow GAAP.

8 MR. TAEBEL: I agree with that, Justice --

9 QUESTION: That's what I thought you meant.

10 MR. TAEBEL: -- Scalia, because --

11 (Laughter.)

12 MR. TAEBEL: I appreciate the assistance, Your
13 Honor.

14 (Laughter.)

15 QUESTION: Mr. Taebel, let me ask you to respond
16 to the question that was raised about this PRM being
17 hundreds of pages, and if the Secretary had to do all of
18 the fine things that she's done in the PRM by regulation
19 we would have regulations of monstrous size, and she would
20 be bogged down all the time, having a manual that gets
21 changed monthly, maybe even weekly, having to go through
22 notice and comment for every -- what is in that big, fat
23 manual that doesn't have to go through notice and comment,
24 and what would have, under your fix on this case?

25 MR. TAEBEL: Your Honor, the Government does

1 complain that they will have to promulgate regulations for
2 every cost item. We don't think that that's the case.

3 Most cost items, as we've been indicating here,
4 are recognized consistent with GAAP. When she wants to
5 promulgate, or she wants to use a different method that
6 deviates from the GAAP approach, that's when she has to go
7 forward with APA rulemaking. She did not do that here.
8 Her method is plainly inconsistent with the prescribed
9 GAAP approach.

10 QUESTION: Do you have any notion about how many
11 items in this manual are inconsistent with GAAP?

12 MR. TAEBEL: I do know, Your Honor, that based
13 on other court decisions, the Secretary has sought to
14 promulgate by regulation several of her manual provisions.
15 That's discussed in the amicus brief. It's a 1991 notice
16 in the Federal Register. She has the ability to do that,
17 but bear in mind, please, that most costs are reported and
18 paid consistent with generally accepted accounting
19 principles. That's exactly why the program utilizes GAAP.

20 QUESTION: Yes, but what if you have a period
21 where there is no answer in GAAP, as I gather is your view
22 from 1966 to 1972, and the Secretary establishes a policy
23 that GAAP later disagrees with. Now, she must
24 automatically follow GAAP even though GAAP is silent up to
25 that point. That's your view.

1 MR. TAEBEL: That's what the regulation says,
2 Your Honor. She has to follow GAAP --

3 QUESTION: Even though, if there was already a
4 regulation on the book which had been interpreted in an
5 interpretive bulletin that had been on the books for
6 several years and no one had questioned, she would
7 nevertheless have to abandon that interpretive bulletin
8 and follow GAAP?

9 MR. TAEBEL: Her regulations control over the
10 manual provision, Your Honor. She has adopted GAAP --

11 QUESTION: But at the time, under my hypothesis,
12 at the time the manual was promulgated it correctly
13 explained what the regulation was.

14 MR. TAEBEL: Actually, it did not, Your Honor.
15 Her method is not even consistent with one of the GAAP
16 methods.

17 QUESTION: Well, I was assuming that as a
18 hypothesis, that nevertheless she would have to change it
19 when GAAP plugged what was previously a loophole.

20 MR. TAEBEL: Once she's adopted GAAP, if GAAP
21 changes she would have to change her regulation.

22 QUESTION: What are you relying on for the
23 proposition -- you're simply saying that the language of
24 413.20 adopts GAAP?

25 MR. TAEBEL: Yes, it does, Your Honor. It

1 refers to, again, standardized definitions, accounting
2 statistics, and reporting practices --

3 QUESTION: Yes, with commas after each of them,
4 so standardized accountings and a number of other things,
5 and you say that incorporates GAAP without any further
6 elaboration?

7 MR. TAEBEL: Yes, and it also indicates, Your
8 Honor, that changes in those methods will not be required
9 in order to determine costs payable under the Medicare
10 program.

11 QUESTION: What if there's a conflict between,
12 say, a standard accounting and a standard statistic, or
13 standard reporting practice?

14 MR. TAEBEL: Well, I think in this case, Your
15 Honor, we rely on GAAP to report our costs, and we claim
16 that when a cost is incurred, according to GAAP, it then
17 must be payable under the Medicare program. We think
18 that's the nexus that the Sixth Circuit found here in the
19 regulatory language.

20 QUESTION: Why isn't the Government's
21 explanation of 413.20 a lot more reasonable than yours?

22 The first sentence, after all, says that the
23 principles require that providers maintain sufficient
24 financial records, and it's speaking of what records have
25 to be maintained, and then the second sentence, the one

1 you're relying on, says standardized definitions, et
2 cetera, are followed. Changes will not be required. We
3 won't make you change your books. You can keep your books
4 the way you've been doing it, but that still doesn't mean
5 that we're going to make our determinations on the basis
6 of those decisions.

7 MR. TAEBEL: But the regulatory provision you're
8 citing, Justice Scalia, continues, and it says, to
9 determine costs payable under the program. That is, if
10 a --

11 QUESTION: It says, changes will not be required
12 in order to determine costs payable, and they're saying
13 that. We're not going to make you change these systems.
14 We can determine your costs without you making any changes
15 in those systems. Just submit this information, although
16 today I guess they said you do have to change them, that
17 you weren't complying, but I had thought they said you can
18 submit it this way, and we'll make any adjustments needed.
19 Why isn't that a reasonable reading of it?

20 MR. TAEBEL: Because in this case, Your Honor,
21 there's no disagreement that this particular loss is a
22 reimbursable cost. The only question we need to answer
23 now is when is that cost payable, and this language here,
24 which is the general rule, indicates that it's payable
25 when it's incurred, basically, and under GAAP, it's

1 incurred in 1985, the year of the refinancing.

2 QUESTION: But what about the last sentence of
3 413.20, which says, essentially the methods of determining
4 costs payable under Medicare involve making use of data
5 available from institutions' basic accounts, as usual, to
6 arrive at equitable and proper payment for services to
7 beneficiaries. That sounds like the Secretary has a good
8 deal of latitude.

9 MR. TAEBEL: The problem with that, though,
10 Mr. Chief Justice, is that she has to promulgate her
11 methods of reimbursement by regulation. She claims that
12 we can report under one method and she can pay under an
13 entirely different method.

14 QUESTION: Why isn't this a promulgation of her
15 system of reimbursement? She's going to arrive at
16 equitable and proper payments.

17 MR. TAEBEL: She is, and it indicates that
18 changes in those practices will not be required in order
19 to determine costs payable.

20 QUESTION: But that's changes in the practices
21 for the hospitals reporting to her. It doesn't say that
22 she's necessarily going to conform exactly to the same
23 principles that may govern the hospital in reporting to
24 her, as I read it.

25 MR. TAEBEL: Your Honor, I think the problem

1 here was articulated in one of the amicus briefs. It
2 talks about the black hole theory. If she's going to pay
3 us under a different method that deviates from the general
4 GAAP approach, she has to put that into regulation form.
5 We don't know what that method is.

6 QUESTION: Why isn't the last sentence of 413.20
7 perfectly good? You know, beggars can't be choosers.
8 You're coming to get some money, and she says she's going
9 to make equitable and proper payments.

10 MR. TAEBEL: That particular sentence, Your
11 Honor, indicates that payment will be made based on our
12 financial reports as usually maintained. The way we
13 usually maintain our books, Your Honor, is according to
14 GAAP.

15 QUESTION: May I ask, Mr. Taebel, following up
16 on the Chief Justice's thought -- all of this is under the
17 subheading of Subpart B. Accounting Methods and Reports
18 is the whole -- what you'd look at, but Subpart C is what
19 deals with limits on cost reimbursement, which is an
20 entirely different subpart, but it does suggest that the
21 regulation thought that reporting information is subject
22 to one set of information and limits on cost reimbursement
23 are in another group, which include things like interest
24 expense, depreciation expense, and all of that, and we're
25 fighting about the treatment of an item of interest

1 expense here.

2 MR. TAEBEL: But prior to 1986, Your Honor, when
3 the regulations were redesignated, 413.20 had been part of
4 former part 405, and the subchapter heading it was under
5 at that time was "Reasonable Cost Reimbursement General
6 Rules."

7 That changed when the designation of the
8 regulations changed, beginning in 1986. The advanced
9 refunding here occurred in 1985. If I can --

10 QUESTION: In effect, you're saying that unless
11 you read 419.20 as a reimbursement reg, the Secretary has
12 not issued adequate regs as required by the statute.
13 That's your major premise.

14 MR. TAEBEL: That is correct, Your Honor.

15 QUESTION: Yes.

16 QUESTION: And what follows as a result of that,
17 when she doesn't issue adequate regs?

18 MR. TAEBEL: Exactly what the Sixth Circuit
19 held, Your Honor, and that is her manual provision, which
20 is a substantive rule, when it conflicts with the
21 regulatory language, is invalid. Therefore, we are
22 entitled to reimbursement for the full Medicare portion of
23 our advanced refunding loss in the year it was incurred,
24 1985.

25 QUESTION: Well, I would think your argument

1 would be that we shouldn't read it to be an invalid reg,
2 that if, indeed, the Secretary would not have complied
3 with the law adequately unless 413.20 is read to be a
4 substantive requirement and not just a reporting
5 requirement, we should not assume that the Secretary was
6 not complying with the law, and therefore we should read
7 it as a substantive requirement. I guess that's your
8 argument.

9 MR. TAEBEL: It is, Your Honor, and we're
10 maintaining that interpretation here should not be
11 deferred to, because it's inconsistent with the plain
12 language of the regulation.

13 QUESTION: The plain language says -- it says
14 that they are followed. It says they are followed, but the
15 language has to do with reporting, so you'd have to imply
16 that the substantive reimbursement also follows it, which
17 is not what it says, but maybe it's a fair implication.
18 But if it's a fair implication, I take it it would be
19 normally. Normally.

20 So what's wrong with their argument that this is
21 unusual, the accounting profession has danced around on
22 this all the time, they've come up both ways, this is
23 unusual, and that's why we went the other way?

24 MR. TAEBEL: The problem with it, Justice
25 Breyer, is that the regulation calls for the GAAP

1 approach, and we are not arguing that the Secretary can
2 choose another method.

3 QUESTION: It calls for it on reporting. It
4 doesn't call for it on reimbursement unless you imply
5 that, I take it.

6 MR. TAEBEL: Well, it indicates that changes in
7 these practices will not be required in order to determine
8 costs payable. We have the argument here that the cost is
9 already reimbursable. There's no dispute about that. The
10 only question is, when is it payable?

11 QUESTION: So doesn't she get some leeway
12 interpreting her own regulation, which is hers, in a way
13 that would be fair, that would allow the whole thing to
14 function well, with 248 million different items of
15 reimbursement, which I take it she couldn't take 10 years
16 to put in regs?

17 MR. TAEBEL: Well, the other problem, Your
18 Honor, besides the plain language, is her interpretation
19 of these regulations. As I indicated, with due respect to
20 the Secretary and Mr. Jones, there has been actually
21 inconsistency across the board on this issue.

22 The prior manual provision that she applied to
23 advanced refunding losses between December 31, 1976, and
24 the issuance of manual provision 233, under that manual
25 provision, Guernsey Memorial Hospital would have been

1 entitled to the full Medicare portion of its advanced
2 refunding loss in the year of the refinancing.

3 That is because, under the prior manual
4 provision 215, Guernsey Memorial's loss qualified as a
5 small loss, which was meaning it was less than 50 percent
6 of what its interest expense otherwise would have been.
7 Therefore, under that manual provision, we would have
8 received the full Medicare portion quite unlike what her
9 treatment is now, when she's issued 233.

10 So we have inconsistencies between 233 and the
11 underlying regulations, we have inconsistencies between
12 233 and manual provision 215, and we also have a problem,
13 I think, just in a vacuum. This manual provision is a
14 substantive rule under the APA because it creates a
15 complicated new method for reimbursing advanced refunding
16 losses.

17 Mr. Jones indicated this Court's decision last
18 term in Thomas Jefferson. I think in stark contrast to
19 the case here, you had a particular regulation dealing
20 with the specific cost item in question there. We don't
21 have any regulation here. All we have is the general
22 regulation indicating that GAAP ought to be followed.

23 The manual provision does not interpret 413.9.
24 We find that somewhat curious, because that regulation
25 reiterates the statutory requirement that she promulgate

1 her methods by regulation.

2 QUESTION: How detailed is that requirement,
3 Mr. Taebel? Why does it extend to this particular item
4 and not to -- you know, you can go very far down into the
5 details of cost accounting. How far down into the details
6 does she have to go? How do we know that this is at a
7 high enough level that really it had to be handled by
8 regulation?

9 MR. TAEBEL: Because, Your Honor, she readily
10 admits that it is inconsistent with GAAP. GAAP prohibits
11 the amortization of the loss.

12 QUESTION: Your position is that any cost
13 accounting principles which the Secretary requires that
14 are contrary to generally accepted accounting principles,
15 at least those must be adopted by regulation?

16 MR. TAEBEL: Yes. She's called for it here in
17 this regulation. We report consistent with GAAP. We put
18 the loss in our tax statement, in our financial reports,
19 and now we suddenly have to come up with a whole new set
20 of bookkeeping requirements for Medicare reimbursement.
21 If she wants to do that, she has to put it in a
22 regulation.

23 I will also add that --

24 QUESTION: Could she get out of it by changing
25 413.20, by not saying that the standardized whatever, that

1 GAAP is the rule unless there's a regulation to the
2 contrary? Could she change 413 to have something other
3 than GAAP apply to what has to be reported?

4 MR. TAEBEL: I believe so, Your Honor. She
5 claims that her interpretation has been, we utilize GAAP
6 unless there's a regulation or a manual provision to the
7 contrary. The problem with that is, she's using a forward
8 to the PRM to apply GAAP so that she can now get out from
9 underneath GAAP to another manual provision.

10 Somewhere along the way here, I think she needs
11 to promulgate her methods of reimbursement by regulation.
12 That's what Congress intended since the inception of the
13 Medicare program in 1965. That's what the plain language
14 of 42 U.S.C. 1395(x)(L)(v)(1)(A) states. It's reproduced at
15 page 2 of the petition.

16 QUESTION: So could she then simply promulgate
17 the manual as it now is, subject to notice and comment,
18 and then that would be a governing regulation?

19 MR. TAEBEL: Yes, she could, Your Honor.
20 However, we would indicate on the record of this case --
21 we certainly don't have much of a record, because we
22 haven't gone through the APA -- but on the record of this
23 case, I think the regulation would still be subject to
24 rationality attacks, because the overwhelming record
25 evidence here indicates that the loss does not relate to

1 future periods.

2 QUESTION: The court of appeals didn't agree
3 with you on that, did it?

4 MR. TAEBEL: The court of appeals -- that's
5 correct, Mr. Chief Justice. The court of appeals
6 indicated the Secretary could make a respectable argument
7 that that type of treatment in a regulation would be
8 rational. However, in this record, the overwhelming
9 evidence indicates that the loss does not relate to future
10 periods, and the hospital doesn't incur any costs related
11 to that loss.

12 QUESTION: The analogy to spending a couple of
13 million dollars to put a new wing on the hospital and
14 depreciating it over the next 10 years is pretty much like
15 this case, isn't it?

16 MR. TAEBEL: No, it's --

17 QUESTION: They spent a lot of money to reduce
18 their future interest expense.

19 MR. TAEBEL: No, it's not, Justice Stevens,
20 because in that case you have an asset on the books.
21 Here, the bonds have been defeased entirely. The
22 hospital's been discharged. There's nothing on the books.
23 The trustee is now --

24 QUESTION: You're not seriously arguing the
25 Secretary's position is irrational. Are you really?

1 MR. TAEBEL: On the record of this case, yes, we
2 are, Your Honor, because the statute --

3 QUESTION: You're never going to sell me on that
4 one.

5 MR. TAEBEL: The statute requires that costs
6 must be incurred.

7 QUESTION: Then, if I understand this, it's
8 rather like a hospital that would say -- suppose you could
9 set up an irrevocable trust with \$1 million in it to
10 prepay meals over the next 10 years -- it might be
11 rational to say you incurred the expense in year 1.
12 That's what you'd like to say. It might also be rational
13 to accrue it as the transaction, namely the meals are
14 delivered, in which case you'd have to amortize it. I
15 take it this is a little bit like that.

16 It's rational to say you incurred the whole
17 prepayment expense when you put it in the trust, or it's
18 rational to say the expense was incurred as the trust paid
19 out the prepaid interest to the original bondholders with
20 their principal.

21 Is that right? I'm asking you to correct me if
22 I'm wrong.

23 MR. TAEBEL: The problem with that, Justice
24 Breyer, is, after the refinancing these costs are on the
25 books of the trustee. They're not on the books of the

1 hospital. These are not costs of the hospital after the
2 refinancing.

3 I think you're referring to a situation where
4 there may have been some relation between the hospital and
5 the escrow fund. There is none here. Those costs after
6 1985 are no longer costs of the hospital.

7 Mr. Jones indicated a decision from the Eighth
8 Circuit in Research Medical Center where interest was
9 capitalized over the life of the asset. In that case,
10 that approach is consistent with GAAP. It's the normal
11 practice. You have interest during construction. You
12 attach it to the underlying asset, and it is amortized,
13 very similar to -- as what Justice Stevens was referring
14 to, depreciation.

15 By analogy, if you sell or dispose of a
16 depreciable asset, since it's off your books, you don't
17 have it any more, you recognize the loss or gain on the
18 sale the time you transfer it. That is the analogy that
19 the Provider Reimbursement Review Board utilized in its
20 opinion in this case.

21 QUESTION: Of course, that opinion wasn't
22 unanimous, either.

23 MR. TAEBEL: Yes, it was, Your Honor.

24 QUESTION: I thought you were referring to the
25 accounting bulletin. That was not unanimous, the GAAP

1 ruling. There were dissents from that.

2 MR. TAEBEL: There were 18 voting members, Your
3 Honor, and 3 dissented, and the dissents are not
4 consistent with the Secretary's position here, either.

5 QUESTION: They do suggest the contrary view is
6 not irrational, at least.

7 MR. TAEBEL: They suggest, Your Honor, that
8 there had been different methods at that time, and that
9 because the loss relates to the prior period, or the
10 period when the refunded bonds were in existence, that's
11 why the APB decided it had to be only one method, and that
12 is, you recognize it currently in income.

13 In conclusion, then, Your Honor, we respectfully
14 request that this Court affirm the decision of the Sixth
15 Circuit below.

16 Thank you.

17 QUESTION: Thank you, Mr. Taebel.

18 Mr. Jones, you have 2 minutes remaining.

19 REBUTTAL ARGUMENT OF KENT L. JONES

20 ON BEHALF OF THE PETITIONER

21 MR. JONES: Thank you.

22 There are two questions of interpretation. The
23 first is whether the Secretary is required by her
24 regulations to apply GAAP in reimbursement determinations.
25 Her consistent and contemporaneous interpretation of the

1 regs has been that it does not.

2 That interpretation has been set out in the
3 manual, which makes quite clear that GAAP applies only if
4 there is no other applicable manual provision. It's been
5 made clear in her litigation over the last 15 years on
6 this subject, and her rational and contemporaneous,
7 consistent interpretation should be given controlling
8 weight in understanding her own regulation.

9 Now, the other question of interpretation is
10 whether the amortization of these types of advance
11 refunding costs are rationally to be related to the
12 periods over which they benefit the hospital by reducing
13 its costs. For the reasons that we've explained, it seems
14 eminently rational. The courts below agreed with that.

15 And not to quibble, but there were three
16 dissents to the GAAP opinion, but one of the part -- one
17 of the members of that opinion who assented to the opinion
18 also believed that amortization would have been proper.

19 This is an issue on which accrual accounting
20 could reach different conclusions, and the conclusion
21 reached by the Secretary as to that substantive question
22 was not unreasonable or arbitrary, and I should point out
23 that in Thomas Jefferson University, when the Court
24 emphasized the deference which the Secretary's decision
25 should be given -- the Court emphasized that these kinds

1 of determinations involve the application of policy
2 judgments to the facts of the --

3 CHIEF JUSTICE REHNQUIST: Thank you, Mr. Jones.

4 MR. JONES: Thank you.

5 CHIEF JUSTICE REHNQUIST: The case is submitted.

6 (Whereupon, at 12:01 p.m., the case in the
7 above-entitled matter was submitted.)

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CERTIFICATION

Alderson Reporting Company, Inc., hereby certifies that the attached pages represents an accurate transcription of electronic sound recording of the oral argument before the Supreme Court of The United States in the Matter of:

DONNA E. SHALALA, SECRETARY OF HEALTH & HUMAN SERVICES, Petitioner
v. GUERNSEY MEMORIAL HOSPITAL

CASE NO.:93-1251

and that these attached pages constitutes the original transcript of the proceedings for the records of the court.

BY *Ann Mari Federico*

(REPORTER)