RENDERED: AUGUST 23, 2013; 10:00 A.M.
NOT TO BE PUBLISHED

Commonwealth of Kentucky

Court of Appeals

NO. 2010-CA-001319-MR

CABINET FOR HEALTH AND FAMILY SERVICES AND JANIE MILLER, SECRETARY OF THE CABINET FOR HEALTH AND FAMILY SERVICES — APPELLANTS

v.

APPEAL FROM HARLAN CIRCUIT COURT
HONORABLE RUSSELL D. ALRED, JUDGE
ACTION NO. 09-CI-00458

REGIONAL HEALTHCARE, INC. D/B/A HARLAN ARH HOSPITAL — APPELLEE

OPINION AND ORDER
GRANTING PARTIAL DISMISSAL
AND REVERSING AND REMANDING

** ** ** ** **

BEFORE: CLAYTON, MOORE, AND NICKELL, JUDGES.

MOORE, JUDGE: This appeal involves a dispute between the Cabinet for Health and Family Services, and Appalachian Regional Healthcare, Inc. d/b/a Harlan ARH ("Harlan"), over the proper way to calculate the per diem Medicaid

reimbursement rate applicable to Harlan's psychiatric "distinct part unit," or "DPU," for the fiscal year of July 1, 2007, to June 30, 2008. At the administrative level, the Secretary of the Cabinet for Health and Family Services, Janie Miller, held that Harlan's per diem reimbursement rate during that period was subject to a total of three different rate-calculating methodologies, applicable at separate intervals, due to a series of regulatory changes that occurred during that period. The Harlan Circuit Court reversed, and the Cabinet and its Secretary now appeal. Upon review, we reverse the Harlan Circuit Court, but remand for further proceedings at the administrative level regarding Harlan's defense of equitable estoppel.

FACTUAL AND PROCEDURAL HISTORY

The issues raised in this appeal have been discussed, addressed, and have evolved over the course of three separate orders in this matter, beginning with the findings of fact, conclusions of law, and recommended order of a hearing officer for the Cabinet. In relevant part, it states:

> FINDINGS OF FACT
>
> 1. Harlan ARH is a regional hospital located in Harlan, Kentucky. It is part of the Appalachian Regional Healthcare system.
>
> 2. Harlan ARH has a separate unit for psychiatric patients, referred to as a Distinct Part Unit ("DPU").
>
> 3. Until 2007, a DPU's Medicaid per diem reimbursement rate for its patients was set by 907

KAR[1] 1:013. Harlan ARH's DPU per diem rate for 2007 for adult patients was $1,273.20.

4. On October 15, 2007, the Cabinet filed an emergency regulation, 907 KAR 1:815E, to provide a new method for calculation of Medicaid reimbursement rates for in-patient hospitals. This included the reimbursement for psychiatric care provided in DPU's.

5. Section 2(1) of 907 KAR 1:815E controlled the method for calculating the per diem rate for hospital based DPU's. Section 2(1)(a) stated that the rates were to be based on the per diem cost at the facility for Medicaid patients on the most recently finalized Medicaid cost report received prior to the rate year.

6. On November 15, 2007, the Cabinet withdrew 907 KAR 1:815E (10/15/07) and filed a new version of the emergency regulation, 907 KAR 1:815E (11/15/07), along with a proposed draft of the ordinary regulation.

7. Section 2(2) of the new 907 KAR 1:815E (11/15/07) set the methodology for the calculation of the per diem rate for rehabilitation based on the most recently received cost report, trended and indexed to the current state fiscal year for rehabilitation. For psychiatric care, the rate is set by the sum of the operating rate and the capital per diem rate.

8. On April 14, 2008, the Cabinet submitted changes to the ensuing ordinary regulation. The ordinary regulation became final and replaced the emergency regulation on June 6, 2008. The final regulation based the rehabilitation and psychiatric per diem rates on the most recently received cost report.

9. On May 16, 2008, the Cabinet sent Harlan ARH a letter informing it that the Cabinet had completed the as submitted cost report for fiscal year ending June 30, 2006. This letter also informed the Appellant that its psychiatric inpatient rates were established in accordance with 907 KAR 1:815, and the new rate of $732.44 would

[1] Kentucky Administrative Regulation.

be effective retroactive to October 19, 2007. This appeal followed.

CONCLUSIONS OF LAW

1. The Health Services Administrative Hearings Branch, Cabinet for Health and Family Services, has jurisdiction in this matter pursuant to 907 KAR 1:671.

2. The Commonwealth of Kentucky, Cabinet for Health and Family Services, is the single state agency, pursuant to 42 U.S.C. Section 1396(a)(a)(5) and KRS[2] 194.030(3), which administers the Medicaid Program in the Commonwealth of Kentucky.

3. The first issue to be resolved in this matter is to determine which regulation applies to the determination made by the Cabinet in its May 16, 2008 decision. At the time that decision was issued, the Cabinet had withdrawn the 10/15/07 version of the emergency regulation, and replaced it with the 11/15/07 version. The ordinary regulation was not adopted until June 6, 2008. In the IDR[3] decision, the Cabinet cites the 10/15/07 version of the regulation. That regulation was withdrawn and was not in effect at the time of the decision. In its brief, the Cabinet contends its decision was based on the June 6, 2008 ordinary regulation. However, that regulation was not in effect at the time of the recalculation and could not have been used as a basis for a determination. The undersigned must conclude that the regulation in effect at the time of the Cabinet's determination was the 11/15/07 version of 907 KAR 1:815E. The ordinary regulation had not yet taken effect and the 10/15/07 version had been withdrawn, leaving the 11/15/07 version the only regulation in place at that time.

4. The Cabinet should have based its rate calculation on the terms of the 11/15/07 emergency regulation. Section 2 of that regulation states:

[2] Kentucky Revised Statute.

[3] As it is used here, "IDR" means "Informal Dispute Resolution."

Section 2. Payment for Rehabilitation or Psychiatric Care in an In-State Acute Care Hospital.

(1) For rehabilitation care in an in-state acute care hospital that has a Medicare-designated rehabilitation distinct part unit, the department shall reimburse:

(a) A facility specific per diem based on the most recently received Medicare cost report received prior to the rate year, trended and indexed to the current state fiscal year; and

(b) In accordance with Sections 6 and 9 of this administrative regulation.

(2) The department shall reimburse for psychiatric care in an in-state acute care hospital that has a Medicare-designated psychiatric distinct part unit on a per diem basis as follows:

(a) Reimbursement for an inpatient psychiatric service shall be determined by multiplying a hospital's psychiatric per diem rate by the number of allowed patient days.

(b) A psychiatric per diem rate shall be the sum of a psychiatric operating per diem rate and a psychiatric capital per diem rate.

1. The psychiatric operating cost-per-day amounts used to determine the psychiatric operating per diem rate shall be calculated for each hospital by dividing its Medicaid psychiatric cost basis, excluding capital costs and medical education costs, by the number of Medicaid psychiatric patient days in the base year.

2. The Medicaid psychiatric cost basis and patient days shall be based on Medicaid

claims for patients with a psychiatric diagnosis with dates of service in the base year. The psychiatric operating per diem rate shall be adjusted for:

a. The price level increase from the midpoint of the base year to the midpoint of the universal rate year using the CMS Input Price Index; and

b. The change in the Medicare published wage index from the base year to the universal rate year.

c.1. A psychiatric capital per diem rate shall be facility-specific and shall be calculated for each hospital by dividing its Medicaid psychiatric capital cost basis by the number of Medicaid psychiatric patient days in the base year.

2. The Medical psychiatric capital cost basis and patient days shall be based on Medicaid claims for patients with psychiatric diagnoses with date of service in the base year.

3. The psychiatric capital per diem rate shall not be adjusted for inflation.

5. Therefore, the undersigned concludes that the Cabinet should have based its rate calculation on the terms of 907 KAR 1:815E (11/15/07), Section 2(2), the regulation that was in effect at the time of the May 16, 2008 decision. The September 28, 2008 IDR decision states that the rates were based on the 10/15/07 regulation, which had been withdrawn and could not be a basis for a determination. Based on this conclusion, for the calculation of the rehabilitation rate for the Appellant's psychiatric DPU, the Cabinet should have used the FYE June 30, 2007 cost report, which was the last report received before the May 16, 2008 decision. For the calculation of the psychiatric treatment rate for the DPU,

the Cabinet should have followed the procedure set in Section 2(2) of the 11/15/07 version of 907 KAR 1:815E. Since this was not done, this portion of the decision must be remanded to the Cabinet for the proper calculation of the DPU's rates based on the June 30, 2007 cost report.

. . .

7. . . . The undersigned concludes that the regulation permits the recalculation of the psychiatric DPU's per diem rate annually based on the universal rate year.

8. The Appellant next argues that the Cabinet exceeded its scope of authority by making the new per diem rates effective on October 15, 2007 by its decision made on May 16, 2008. The Appellant claims this retroactive application violates Section 9(3) of 907 KAR 1:815E. The Cabinet's brief does not address the issue, except to say that the recalculated rate was effective October 15, 2007, the effective date of the first emergency regulation.

9. Section 9 of 907 KAR 1:815E (11/15/07) applies to the calculation of the DPU's rate, pursuant to section 2(1)(b). Section 9(3) states that "(A) prospective rate shall not be subject to retroactive adjustment except for: (a) A critical access hospital; (b) A facility with a rate based on un-audited data." It is uncontested that Harlan ARH does not fall into either of the exceptions to this provision.

10. In general, no statute or regulation is construed to be retroactive, unless expressly declared. See KRS 446.080(3). Retroactive application has been allowed by Kentucky courts if the act was remedial in nature and in line with stated legislative intent. Spurlin v. Adkins, 940 S.W.2d 900 (Ky. 1997). In this matter, however, we have the opposite. The promulgators of the regulation have specifically declared that a prospective rate is not subject to retroactive adjustment. Therefore, the undersigned must conclude that the Cabinet acted in excess of its authority by making the May 16, 2008 calculation of the DPU's per diem effective on October 15, 2007.

11. Since the Cabinet cannot make the recalculated rate effective on October 15, 2007, the undersigned must determine the appropriate effective date. Section 2 of 907 KAR 1:815E (11/15/07) indicates that the Cabinet should set the rates for the current state fiscal year. Section 2(2) of 907 KAR 1:815E indicates that the rate is to be adjusted for the "universal rate year." Section 1(23) defines that term as being a 12 month period beginning in July of each year. This coincides with the state's fiscal year. The undersigned concludes that the rate can only be set prospectively for the next universal rate year. In this case, the remanded calculation should take effect from July 1, 2008 to June 30, 2009, the next universal rate year after the recalculation of the rates.

12. The Appellant next argues that the Cabinet should be estopped from retroactively adjusting its rates. Given the above recommendation, it is not necessary to reach this issue.[4]

13. As its final argument, the Appellant argues that the Cabinet exceeded its statutory authority by restricting the allowable amount of depreciation for buildings and fixtures to 65% of the depreciation listed on the facility's cost report.[5] The Appellant claims this violates KRS 205.560(2), which states that the Cabinet's Medicaid payments "shall be on bases which relate [to] the amount of the payment to the cost of providing the services or supplies."

14. The Cabinet counters that the statute does not require that Medicaid pay 100% of the stated cost, only that it use a basis related to the reported cost. In this case, Medicaid decided to pay 65% of [the] reported cost, thus shifting responsibility for a portion of capital costs to

[4] As discussed later in this opinion, Harlan has raised the defense of equitable estoppel at every level in this matter. No tribunal has addressed it yet.

[5] Although not referenced in the recommended order, the regulation at issue was 907 KAR 1:815 § 15, which provided that "The allowable amount for depreciation on a hospital building and fixtures, excluding major movable equipment, shall be sixty-five (65) percent of the reported depreciation amount as shown in the hospital's cost reports." This regulation, containing identical language, has since been re-codified as 907 KAR 10:815 § 15.

other payors instead of the government. The Cabinet cites 42 USC § 1396(a)(30)(A), which requires that the state program provide payment in a manor [sic] to safeguard against unnecessary utilization.

17. [sic] The undersigned agrees with the Cabinet. An administrative agency may interpret and apply a statute as long as its interpretation is not inconsistent with the terms of the statute. In this case, the Cabinet has provided for payment for capital costs in a manner that is related to the cost reported by the facility, but equally employs its mandate to safeguard against capital expansion that leads to underutilization. The undersigned concludes that the Cabinet has not exceeded it's [sic] authorization as it applies to this Appellant.

RECOMMENDED ORDER

Based on the foregoing Findings of Fact and Conclusions of Law, it is RECOMMENDED that the May 16, 2008 calculation of Harlan ARH psychiatric distinct part unit per diem rates, and the September 28, 2008 IDR decision upholding those rates, be VACATED and REMANDED in part, for calculation of the psychiatric inpatient rates in a manner consistent with this opinion. It is further RECOMMENDED that the Cabinet's decision be AFFIRMED in part, for its decision that the per diem rates for psychiatric DPU's may be recalculated annually, and AFFIRMED in part, in that 907 KAR 1:815E, Section 15, does not exceed the scope of statutory authority. Lastly, it is RECOMMENDED that the Cabinet's decision to retroactively apply the per diem rates to October 15, 2007 be REVERSED in part.

After the hearing officer entered his recommended order, the Cabinet and Harlan ARH filed exceptions with the Secretary. Harlan's exceptions dealt with the portion of the recommended order that upheld the validity of 907 KAR 1:815 § 15, the regulation promulgated by the Cabinet that restricted the allowable amount of depreciation for buildings and fixtures to 65% of the depreciation listed

on Harlan ARH's cost report. Previously, Harlan had urged that this section of the regulation was not rationally related to a legitimate state purpose, and that Kentucky's Medicaid program should pay for 100% of all depreciation costs attributable to the provision of Medicaid services. The basis of Harlan's exception was that no evidence of record supported that this regulation had been promulgated "to safeguard against capital expansion that leads to underutilization," which was the purpose that the hearing officer had cited in support of the regulation's legitimacy and validity.

The Cabinet, on the other hand, filed exceptions to the portion of the recommended order that addressed which regulation and cost report was to be used to determine the calculation of the July 1, 2007-June 30, 2008 per diem Medicaid reimbursement rate for Harlan ARH's psychiatric distinct part unit. The Cabinet urged that Harlan's reimbursement rates had never actually been "retroactively rebased" as Harlan and the hearing officer had represented. The Cabinet explained:

> The following is the process used by the Department in rate setting, has been used for years and was used by the Department in setting the Harlan ARH rate:
>
> 1. There is a universal rate year, coinciding with the state fiscal year. Rates are set at the beginning of the universal rate year. The appropriate cost report to be used in rate setting is that cost report designated for use by the regulation, whether that be the latest available or the latest audited cost report, at the beginning of the rate period.

> 2. An applicable regulation providing for the rate must be in place at the beginning of the rate year. Not only is this necessary for the Cabinet and the provider, but it is also necessary for purpose [sic] of obtaining federal financial participation as required by the Centers for Medicare and Medicaid Services for approval of State Plan Amendments and under the provisions of KRS 205.520(3), KRS 205.560(1) and KRS 194A.050(1).
> 3. "Prospective" rates are not adjusted to correspond to changes in costs reflected in subsequent cost reports. It is, however, common practice to correct errors which may have been made in rate setting. The prospective rate arrived at is then a corrected rate which is still a prospective rate. Certainly if the error was corrected in a manner which benefited the provider, there would be no appeal. It is also fairly common practice, as was done in this case, to set an interim prospective rate, with the final prospective rate set at a later point in time during the universal rate year.
>
> 4. If a regulatory change is made which creates a new basis for the prospective rate, a new rate is calculated using the effective date of the new regulatory provisions. If there are multiple regulatory changes affecting the rate setting, there may be multiple prospective rates set for the same universal rate year but all beginning with the effective date of the amended regulations.
>
> 5. Prospective rates are frequently set after the beginning of the rate period, and sometimes well after the beginning of the rate period. The setting of a prospective rate after the universal rate year started has been the practice in Medicaid for many years. This has never been considered to be a "retrospective" rate setting previously, and to do so would be applying a policy and regulation not currently used or legally required. . . .

With that said, the Cabinet argued that the two emergency regulations touched upon in the hearing officer's order had, upon their effective dates, operated to create two additional rate periods between July 1, 2007, and June 30,

2008. The first was a rate period lasting from October 15, 2007 to November 14, 2007 while 907 KAR 1:815E, promulgated October 15, 2007, was effective; pursuant to Section 2(1)(a) of that version of the regulation, the applicable reimbursement rate for that period was to be calculated "[o]n a facility specific per diem basis equivalent to the per diem cost reported for Medicare distinct part unit patients on the most recently finalized Medicare cost report received prior to the rate year[.]" The second was a rate period lasting from November 15, 2007 to June 30, 2008 while the substance of 907 KAR 1:815E, promulgated November 15, 2007, was effective;[6] and, pursuant to Section 2(1)(a) of that version of the regulation, the facility specific per diem was to be calculated "based on the most recently received Medicare cost report received prior to the rate year, trended and indexed to the current state fiscal year[.]"

After reviewing these exceptions, the Secretary entered a final administrative order holding in relevant part:

> I reject so much of the Hearing Officer's decision that directs DMS[7] to calculate the DPU rate using only the November 15, 2007 version of 907 KAR 1:815E. The

[6] As noted in the hearing officer's order, the version of 907 KAR 1:815E promulgated on November 15, 2007, expired when the ordinary administrative regulation, 907 KAR 1:815, was promulgated on June 8, 2008. In a footnote in its brief, Harlan argues that by the Cabinet's logic yet *another* rate period (*i.e.*, from June 8, 2008, until June 30, 2008) must have come into being as a result of this regulatory change. However, if an additional rate period had come into being in this manner, the methodologies for calculating the applicable rate for that period would have been the same as the methodologies specified in the November 15, 2007 version of 907 KAR 1:815E. As noted in the preamble of the November 15, 2007 emergency regulation, the November 15, 2007 emergency version of this regulation was identical in all respects to the June 8, 2008 ordinary version.

[7] "DMS" refers to the Cabinet for Health and Family Services, Department for Medicaid Services.

> rate must be calculated utilizing the regulation in effect at the time. Three regulations were in effect for the rate year beginning July 1, 2007 and ending June 30, 2008. Consequently, the rate must be calculated in three distinct parts in accordance with the regulation in effect at the time. These time periods are: (1) July 1, 2007-October 14, 2007; (2) October 15, 2007-November 14, 2007; and (3) November 15, 2007-June 30, 2008. The case is remanded to DMS and it is directed to calculate a rate for each of these time periods, employing the regulation in effect during that time.[8]
>
> I adopt the Hearing Officer's conclusion that the DMS did not exceed its authority by restricting the allowable amount of depreciation for buildings and fixtures to 65% of the depreciation listed on the facility's cost report.

Harlan thereafter filed an action in Harlan Circuit Court pursuant to KRS 13B.140 and KRS 418.040 to contest the Secretary's final order. Its arguments were three-fold. First, Harlan maintained that the promulgation of the two emergency versions of 907 KAR 1:815 did not operate to create two additional rate periods with separate reimbursement rates mid-way through the universal rate year of July 1, 2007 to June 30, 2008, and that the substance of those regulations actually precluded the Cabinet from adjusting Harlan's $1273.20 reimbursement

[8] At the circuit court level and in its brief on appeal, Harlan has repeatedly pointed out that 907 KAR 1:671 § 9(13) specifically limits issues that can be raised at the administrative level to those issues raised in the dispute resolution process, and that the period between July 1, 2007 and October 14, 2007, inasmuch as it related to Harlan's applicable rate of reimbursement, was never at issue until it was mentioned in the Secretary's final administrative order. To the extent that Harlan points to this as an example of error, and to the extent that the circuit court reversed this portion of the Secretary's final administrative order, we agree that the Cabinet's failure to raise this as an issue at the administrative level precluded the Secretary from considering it or ordering a recalculation of Harlan's reimbursement rate for that time period. Be that as it may, it appears that the Secretary's order merely instructed DMS to do something that DMS had already done. As recited in the Hearing Officer's recommended order, DMS had already calculated Harlan ARH's $1,273.20 DPU per diem rate for 2007 according to the methodology specified in 907 KAR 1:013, which was the applicable regulation in effect for the period of July 1, 2007 to October 14, 2007.

rate to anything other than $1273.20 until the start of the next universal rate year on July 1, 2008. Second, Harlan argued that if the promulgation of those regulations did cause the result specified in the Secretary's final order, the doctrine of equitable estoppel nevertheless precluded the Cabinet from applying that result to change Harlan's $1273.20 reimbursement rate until July 1, 2008. Third, Harlan argued that the "65%" limitation specified in 907 KAR 1:815 § 15 or in any of the other incarnations of that regulation[9] was arbitrary, in violation of KRS 205.560(2), and that the applicable depreciation rate should be 100%.

Subsequently, the circuit court entered an order reversing the Secretary's final order. In total, the circuit court's order states:

> Appellant/Petitioner Appalachian Regional Healthcare, Inc. d/b/a Harlan ARH Hospital, by counsel, having filed a Petition for Appeal and Declaratory Relief with the Court in the above action, and the Court being otherwise sufficiently advised, IT IS HEREBY ORDERED AND ADJUDGED that Appellant/Petitioner's Petition is GRANTED, and the Final Order of the Secretary is REVERSED, with instructions to adopt the Hearing Officer's Recommended Decision finding that the Psych DPU rates could only be reset or rebased at the beginning of the next universal rate year, July 1, 2008;
>
> IT IS FURTHER ORDERED AND ADJUDGED that Appellant/Petitioner is entitled to judgment REVERSING the Secretary and the Hearing Officer and DECLARING that the provision of the regulation providing that the "allowable amount for depreciation on a hospital building and fixtures, excluding major movable equipment, shall be sixty-five (65) percent of the reported depreciation amount as shown in the hospital's cost reports" impermissibly reduces the amount of depreciation expenses paid by the Cabinet in

[9] *See* Note 5.

> violation of KRS 205.560(2). In rebasing the Psych DPU rates on July 1, 2008, and thereafter the Cabinet shall include 100 percent of the Hospital's depreciation costs attributable to the provision of services and supplies to Medicaid beneficiaries.

This order offers no other insight into why the circuit court decided to reverse the Secretary's final administrative order. Thereafter, the circuit court denied the Cabinet's CR[10] 59.05 motion to alter, amend or vacate the above-referenced order, and this appeal followed.

THE CABINET'S MOTION FOR PARTIAL DISMISSAL

Before we address the substance of this appeal, we must first address a motion that the Cabinet filed with this Court. By way of background, the appellate brief that the Cabinet tendered contains an argument contesting the circuit court's latter conclusion of law, *i.e.*, that the

> allowable amount for depreciation on a hospital building and fixtures, excluding major movable equipment, shall be sixty-five (65) percent of the reported depreciation amount as shown in the hospital's cost reports" impermissibly reduces the amount of depreciation expenses paid by the Cabinet in violation of KRS 205.560(2). In rebasing the Psych DPU rates on July 1, 2008, and thereafter the Cabinet shall include 100 percent of the Hospital's depreciation costs attributable to the provision of services and supplies to Medicaid beneficiaries.

Shortly afterward, the Cabinet filed a motion styled "Cabinet's Motion to Withdraw Appeal on One Issue." In relevant part, its motion provides:

[10] Kentucky Rule of Civil Procedure.

> Comes the Cabinet for Health and Family Services and Janie Miller, the Secretary of the Cabinet for Health and Family Services ("Cabinet"), by counsel, and respectfully moves this Honorable Court to permit it to withdraw its appeal on the following issue raised at II. Of the Cabinet's argument on pages nine (9) through twelve (12), entitled, "The Inpatient Psychiatric Reimbursement Methodology is Consistent with State Law and Regulations." The reason for this motion is as follows:
>
> It was recently discovered that applying that portion of the administrative regulation, 907 KAR 1:018[11] which reduced depreciation costs by [sic] sixty-five percent to distinct part units ("DPU") of a hospitals [sic] costs was contrary to the Cabinet's interpretation of the regulations. In other words, the Department of Medicaid Services does not as a matter of interpretation of its own administrative regulation reduce depreciation costs to sixty-five percent (65%) on DPUs. Undersigned counsel notified counsel for the Appellee of this mistake and advised that a correction to the calculation for the rate years in question would be made and the amount due and owing to the Appellee will be made. Undersigned counsel also advised Appellee's counsel that it will be seeking to drop its appeal of that issue in this case.

The Cabinet's reasons underpinning its motion are puzzling. The Cabinet is prohibited from modifying or limiting any of its administrative regulations through "internal policy, memorandum, or other form of action." *See* KRS 13A.130(1)(a) and (b). And, its statements to the effect that it either simply interprets "65%" to mean "100%," or that it simply chooses not to apply this regulation in a context where it plainly applies,[12] seems to fly in the face of that

[11] 907 KAR 1:018, entitled "reimbursement for drugs," is unrelated to any issue presented in this matter, and its appearance in the Cabinet's motion is an apparent typographical error. Given the context of the Cabinet's motion and the Cabinet's reference to the "65%" provision which only existed in 907 KAR 1:815 § 15 at the time the Cabinet filed its motion, the regulation that the Cabinet intended to reference was the June 8, 2008 version of 907 KAR 1:815.

[12] As Harlan notes in its response to the Cabinet's motion, the "65%" limitation in 907 KAR 1:815 §15 (now 907 KAR 10:815 § 15) is written to apply without exception to various rate

rule. Nevertheless, it is not the prerogative of this Court to require the Cabinet to appeal the circuit court's order on this point if the Cabinet is unwilling to do so. Therefore, the Cabinet's motion is GRANTED, and we will disregard the Cabinet's sole argument, as it appears on pages 9 through 12 of its brief, challenging the circuit court's above-referenced holding.

As an aside, we are granting the Cabinet's motion over Harlan's objection that, in allowing the Cabinet to unilaterally dismiss this part of its own appeal, this Court would effectively be allowing the Cabinet to maintain that 907 KAR 1:815 § 15 (now 907 KAR 10:815 § 15) remains valid. Harlan's objection is unfounded. If a Kentucky administrative regulation is challenged in court, the promulgating administrative body bears the burden of proof to demonstrate the validity of the regulation. *See* KRS 13A.140. The Cabinet's failure to oppose the circuit court's conclusion that this section of its regulation is invalid is not only a failure on the part of the Cabinet to sustain its burden of proof; it is a confession that the circuit court's holding was correct. *See, e.g., Osborne v. Payne*, 31 S.W.3d 911, 916 (Ky. 2000) ("Any part of a judgment appealed from that is not briefed is affirmed as being confessed.").

Having disposed of the Cabinet's motion, we will now proceed with our substantive review of the Cabinet's appeal.

---

setting methodologies for six different types of services, including: 1) inpatient psychiatric or rehabilitation care in a DPU (*see* 907 KAR 10:815 § 2(1)); 2) inpatient psychiatric or rehabilitation care in a non-DPU (*see* § 2(2)); 3) in-state care in a freestanding psychiatric, rehabilitation or long-term acute care hospital (*see* § 3); 4) newly participating freestanding psychiatric, rehabilitation or long-term acute care hospitals (*see* § 4); 5) critical access hospitals (*see* § 5); and 6) out-of-state psychiatric or rehabilitation care (*see* § 16).

ANALYSIS

At the onset, the Cabinet argues that the circuit court proceedings should have been entirely dismissed on the ground of improper venue. As to where the Cabinet preserved this argument, the Cabinet points out that it raised "improper venue" as a defense in its answer to Harlan's initiating complaint below. A search of the record confirms that the only instance where the Cabinet raised the issue of venue was in its answer; the Cabinet never moved to dismiss Harlan's action on the basis of venue; and, the circuit court never addressed the issue of venue.

Merely including "improper venue" as a defense in an answer is not enough. In order to preserve any issue for appellate review, let alone the issue of venue, the Cabinet was obligated to seek and secure a ruling upon it from the circuit court prior to appealing. *See, e.g., Hutchings v. Louisville Trust Co.*, 276 S.W.2d 461, 466 (Ky. 1954) ("[I]t is the accepted rule that a question of law which is not presented to or passed upon by the trial court cannot be raised here for the first time."); *Hatton v. Commonwealth*, 409 S.W.2d 818, 819-20 (Ky.1966) ("The appellate court reviews for errors, and a nonruling cannot be erroneous when the issue has not been presented to the trial court for decision."); *Time Finance Co. v. Beckman*, 295 S.W.2d 346, 349 (Ky. 1956) ("failure to obtain a decision on the objection constitutes a waiver thereof"). Because the Cabinet failed to do so, this allegation of error is wholly unpreserved and warrants no further discussion.

Next, the Cabinet asserts that the order entered by the circuit court demonstrates that the circuit court "abdicated its decision-making responsibility" because it includes no rationale supporting its holdings and was actually the very order tendered to it by Harlan. Even if something beyond the Cabinet's speculation supported that the circuit court had abdicated its decision-making authority, however, this in and of itself would not rise to the level of error requiring remand. The only remaining issue that the Cabinet has presented for our review is an issue of legal interpretation, namely, whether the Cabinet's promulgation of multiple versions of 907 KAR 1:815 during the period between July 1, 2007, and June 30, 2008, effectively subjected Harlan to three different reimbursement rates (*i.e.*, its original rate of $1273.20, applying from July 1, 2007 until October 14, 2007; a rate calculated pursuant to the methodology of the October 15, 2007 emergency version of 907 KAR 1:815, applying from October 15, 2007 until November 14, 2007; and, a rate calculated pursuant to the methodology of the November 15, 2007 emergency version of 907 KAR 1:815, applying from November 15, 2007 until June 30, 2008). Because this is merely a legal issue, our review is in no way dependent upon or deferential to the circuit court's initial review of it. Stated differently, we review the circuit court's conclusions of law *de novo*. *Stipp v. St. Charles*, 291 S.W.3d 720, 723 (Ky. App. 2009).

The Cabinet's final argument is that the circuit court erred when it reversed the Secretary and directed Harlan's reimbursement rate for that period to be calculated consistently with the analysis set forth in the hearing officer's prior

recommended order. As indicated, the Cabinet argues that the Secretary correctly determined Harlan was subject to not one but three separate reimbursement rates during the period of July 1, 2007, to June 30, 2008, corresponding to the effective dates of the applicable regulations.

Before we address the Cabinet's argument, it is important to first note what is not at issue in this matter. To be clear, Harlan has never challenged the validity of any part of 907 KAR 1:815 and its several versions and emergency versions, aside from the previously-discussed Section 15 of that regulation. Thus, with the exception of that section, we presume the remainder of this regulation is valid. *See* KRS 13A.140(1) ("Administrative regulations are presumed to be valid until declared otherwise by a court . . . "). Also, Harlan has never argued that the Cabinet improperly invoked or failed to follow KRS 13A.190, the applicable procedure for promulgating emergency regulations, when it promulgated its versions of 907 KAR 1:815E on October 15, 2007, and November 15, 2007. Therefore, we presume those procedures were properly observed by the Cabinet.

Furthermore, Harlan has never argued that the Cabinet lacked the statutory authority to promulgate multiple regulations capable of altering, as of their effective dates and prospectively thereafter until superseded, a provider's reimbursement rate mid-way through any given universal rate year. To the contrary, Harlan has conceded that the Cabinet does have the authority to do so, and Harlan has actually appended to its brief a copy of an unrelated emergency

regulation, 907 KAR 1:013E[13] (effective October 15, 2007, and withdrawn on November 15, 2007), to underscore that the Cabinet has indeed done so in similar contexts.

Boiled down, Harlan only argues that the Cabinet acted in excess of its authority by changing Harlan's reimbursement rate mid-way through the universal rate year of July 1, 2007, to June 30, 2008, because of the *wording* of 907 KAR 1:815 and its emergency versions. Specifically, Harlan contends that those regulations as written do not support the Secretary's interpretation that, as of the date that those regulations were promulgated, the rates specified in those regulations were also intended to become immediately effective. As its sole support for this argument, Harlan points to the copy of 907 KAR 1:013E that it has appended to its brief. Harlan points out that this regulation included in several places the phrase "for a rate effective upon the effective date of this administrative regulation,"[14] but that no such phrase appears in any version or emergency version of 907 KAR 1:815. Based upon this omission, Harlan reasons that the Cabinet therefore did not intend for the substance of 907 KAR 1:815E, either the October 2007 version or November 2007 version, to become effective until July 1, 2008.

We have not located any other regulation that includes that phrase. Nevertheless, in the context of an emergency regulation, it would simply be

[13] This emergency regulation was entitled "Diagnostic-related group (DRG) inpatient hospital reimbursement." It was the predecessor of what is now 907 KAR 10:825, entitled "Diagnosis-related group (DRG) inpatient hospital reimbursement."

[14] In particular, this phrase was included in 907 KAR 1:013E, §§ 2(3)(b), 2(5)(c), 2(14)(a)(2), 2(14)(b)(2), 2(14)(d)(1)(b), 2(14)(e)(1)(a), and 2(14)(e)(2)(b).

redundant to include it in any event. Given their urgent nature, emergency regulations "must be placed into effect *immediately*[.]" KRS 13A.190(1)(a) (emphasis added). Specifically, they must be placed into effect immediately in order to: 1) "Meet an imminent threat to public health, safety, or welfare" (KRS 13A.190(1)(a)(1)); 2) "Prevent a loss of federal or state funds" (KRS 13A.190(1)(a)(2); 3) "Meet a deadline for the promulgation of an administrative regulation that is established by state law, or federal law or regulation" (KRS 13A.190(1)(a)(3); or 4) "Protect human health and the environment" (KRS 13A.190(1)(a)(4)). Moreover, because of the urgent and immediate nature of emergency regulations, it would be absurd to interpret either the October 2007 or November 2007 emergency version of 907 KAR 1:815 to mean that the reimbursement rates specified in either of those emergency regulations would only be effective starting July 1, 2008; indeed, both of these emergency regulations would have expired before that date had even arrived. *See* KRS 13A.190(3)(a) (providing that emergency regulations generally expire "one hundred eighty (180) days after the date of filing or when the same matter filed as an ordinary administrative regulation filed for review is adopted, whichever occurs first").

In short, we find no error in the Secretary's interpretation of how the regulatory changes between July 1, 2007, and June 30, 2008, affected Harlan's reimbursement rate.

As a side note, Harlan asserts that if the Cabinet's changes to 907 KAR 1:815 from June 30, 2007 through July 1, 2008, did have the effect of

creating three separate reimbursement rate periods subject to different methodologies during that time, a rather awkward result ensues. As Harlan explains in its brief:

> The October 15, 2007 version of [907 KAR 1:815] provided that the rate had to be set based on a "finalized" cost report. The [fiscal year] June 30, 2006 Cost Report the Cabinet used had not been audited or "finalized". The wording in the November 15, 2007 regulation was changed so that a new rate would be calculated based on the latest cost report "received" meaning it did not have to be an audited cost report. . . . Because of the often lengthy delays in auditing cost reports, the Secretary's Final Order, if followed, would result in the new October 15, 2007, and the new November 15, 2007 rates being rebased on cost reports that were years apart.

We are not unsympathetic if the regulatory scheme created by the Cabinet has created a level of difficulty. To the extent that Harlan raises this as any kind of argument on appeal it must be rejected because "it is not the province of a court to judge the wisdom of the regulatory authority. Our concern is whether it has exceeded its power." *Hopwood v. City of Paducah*, 424 S.W.2d 134, 136 (Ky. 1968).

Harlan also contends that we could alternatively affirm the circuit court's order on the basis of equitable estoppel. It is true that Harlan has properly raised and preserved this defense at every stage of the administrative and circuit court proceedings.[15] Also, in exceptional circumstances, Kentucky recognizes that

[15] We pause to note that it was not necessary for Harlan to have filed any kind of protective cross-appeal on this issue. Moreover, the record is abundantly clear that Harlan preserved this issue, and the Cabinet has not argued otherwise. "Judicial economy requires that a party actually raise an issue for it to be treated as live on appellate review; it does not require that a prevailing party use what amounts to a separate appeal to maintain an ongoing dispute over an issue that

equitable estoppel can be applied against a state agency, such as the Cabinet, and can be used to estop an administrative agency from performing its statutory duties. *See Board of Trustees, Kentucky Retirement Systems v. Grant*, 257 S.W.3d 591, 594–5 (Ky. App. 2008).[16] However, "the existence of an equitable estoppel claim is a question of fact. The determination of that fact is first the responsibility of the hearing officer, KRS 13B.090(1), .110(1), and then the Board [or Agency Head]. KRS 13B.120(2), (3)." *Grant*, 257 S.W.3d at 595. Thus, we are precluded from considering Harlan's claim of equitable estoppel until it has been ruled upon at the administrative level, and we must remand this matter for that purpose.

CONCLUSION

The Cabinet's motion to withdraw its appeal on one issue is GRANTED.

As it relates to the remainder of this appeal, the Secretary's interpretation of Harlan's reimbursement rate is consistent with the applicable statutes and regulations. Therefore, the portion of the circuit court's order to the contrary is REVERSED. Nevertheless, Harlan remains entitled to a ruling upon its claim of equitable estoppel and we therefore REMAND this matter to the administrative level for that purpose.

ALL CONCUR.

---

was raised but, for whatever reason, not decided below." *Fischer v. Fischer*, 348 S.W.3d 582, 597 (Ky. 2011).

[16] Equitable estoppel cannot be applied against a state agency absent exceptional circumstances involving gross inequity. *Grant*, 257 S.W.3d at 594. The Court in *Grant* noted that *Board of Trustees v. Ray*, 2003 WL 1227585 (Ky. App., Jan. 24, 2003) provides guidance in determining what qualifies as an exceptional circumstance.

ENTERED: August 23, 2013

/s/ Joy A. Moore
JUDGE, COURT OF APPEALS

BRIEF FOR APPELLANT:

Ann Truitt Hunsaker
Frankfort, Kentucky

BRIEF FOR APPELLEE:

Stephen R. Price, Sr.
Carole D. Christian
John W. Woodard, Jr.
Louisville, Kentucky