

IN THE CLAIMS COMMISSION OF THE STATE OF TENNESSEE  
MIDDLE DIVISION

CADLEROCK JOINT VENTURE, II, L.P., )  
 )  
 CLAIMANT, )  
 )  
 VS. ) CLAIM NO. K20081073  
 )  
 STATE OF TENNESSEE, )  
 )  
 DEFENDANT. )

**FILED**

AUG 04 2009  
Tennessee Claims Commission  
CLERK'S OFFICE

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**ORDER GRANTING MOTION TO DISMISS**

This matter is before the Commission on the State's motion to dismiss for lack of subject matter jurisdiction. Claimant, Cadlerock Joint Venture, II, L.P. ("Cadlerock"), has opposed the motion.

**FACTUAL BACKGROUND**

Cadlerock is a secured creditor of Life Action of Tennessee, Inc. ("Life Action"), a former TennCare provider. Life Action had a Provider Agreement with the State of Tennessee, Department of Finance and Administration, Division of Mental Retardation Services and the Bureau of TennCare to provide services to persons with mental retardation. As a part of its operations, Life Action secured a loan from the Bank of Nashville, which was collateralized by Life Action's accounts receivable,

including the proceeds due from the State. At some point, the loan was apparently assigned by the Bank of Nashville to Cadlerock, which notified Life Action of the assignment.

During the term of the contract with the State, Life Action defaulted on the secured debt to Cadlerock. Cadlerock alleges that it notified the State of its secured interest and Life Action's default and requested that the State pay its contractual obligation to Life Action directly to Cadlerock as required by Tenn. Code Ann. § 47-9-406(a) of the Uniform Commercial Code ("UCC"). Cadlerock contends that the State ignored its demand and refused to honor its assignment, instead continuing to pay Life Action under the contract.

Cadlerock sues for the State's violation of its rights under the UCC, for common law conversion, and for negligence. It seeks damages of \$622,252.70 as well as attorneys fees and expenses.

In its motion to dismiss, The State contends the legislature has not authorized Cadlerock's action against it for violation of the UCC, common law conversion or negligence and that the State therefore retains its immunity from such claims. In addition, it argues that to the extent that

Tenn. Code Ann. § 47-9-607(a)(1) would require that the State honor Cadlerock's assignment, it is preempted by the anti-assignment provision of the federal Medicaid law, 42 U.S.C. § 1396a (a)(32) and its corresponding implementing regulations.

## DISCUSSION

### CLAIMS COMMISSION JURISDICTION

Subject matter jurisdiction concerns the authority of a court to hear a controversy. *Meighan v. U.S. Sprint Commc'ns*, 924 S.W.2d 632, 639 (Tenn. 1996). Subject matter jurisdiction involves the nature of the cause of action and the relief sought, and can only be conferred on a court by constitutional or legislative act. *Northland Ins. Co. v. State*, 33 S.W.3d 727, 729 (Tenn. 2000).

When subject matter jurisdiction is at issue, the court must ascertain the nature or gravamen of the pending action. *Brandy Hills Estates, LLC v. Reeves*, 237 S.W.3d 307, 315 (Tenn.Ct.App. 2006). Once that is determined, the court must determine whether the Constitution of Tennessee, the General Assembly, or the common law have conferred the power to adjudicate cases of that sort on the court. *Id.*

The State of Tennessee, as a sovereign, is immune from suit except as it consents to be sued. *Stewart v. State*, 33 S.W.3d 785, 790 (Tenn. 2000). The Claims Commission is a forum of limited jurisdiction and its authority to render damages against the State is limited to claims based on the acts or omissions of state employees, as defined in Tenn. Code Ann. § 8-42-101(3), which fall within certain categories. The categories of claims over which the Claims Commission has jurisdiction are outlined in Tenn. Code Ann. § 9-8-307(a). If a claim falls outside of the categories specified in § 9-8-307(a), then the state retains its immunity from suit, and a claimant may not seek relief from the State. *Stewart v. State*, 33 S.W.3d 785, 790 (Tenn. 2000). When deciding whether the Commission has jurisdiction to hear a claim under the statute, a liberal construction in favor of jurisdiction must be given, “but only so long as (1) the particular grant of jurisdiction is ambiguous and admits of several constructions, and (2) the ‘most favorable view in support of the petitioner’s claim’ is not clearly contrary to the statutory language used by the General Assembly. *Stewart v. State*, 33 S.W.3d 785, 791.

The State argues that Cadlerock's action to enforce its assignment right under the Uniform Commercial Code, Tenn. Code Ann. § 47-9-601, does not fall into any of the categories in Tenn. Code Ann. § 9-8-307(a) over which the Commission has subject matter jurisdiction. In response, Cadlerock has identified Tenn. Code Ann. § 9-8-307(a)(1)(L), relative to breach of a written contract, and Tenn. Code Ann. § 9-8-307(a)(1)(N), relative negligent deprivation of statutory rights, as the jurisdictional bases for this action.

**I. Breach of a written contract,**  
**Tenn. Code Ann. § 9-8-307(a)(1)(L).**

The Claims Commission's jurisdiction over contract actions is limited to "[a]ctions for breach of a written contract between the claimant and the state which was executed by one (1) or more state officers or employees with authority to execute the contract..." Tenn. Code Ann. § 9-8-307(a)(1)(L). The Commission's exercise of jurisdiction under this provision therefore requires a finding that: (1) there was a written contract between Cadlerock and the State; and (2) that the contract was executed by one or more state officers or employees with authority to execute the contract.

Cadlerock does not allege that it was a party to the contract at issue, which was between the Department of Finance, Division of Mental Retardation Services and the Bureau of TennCare and Life Action. (Complaint, exhibit 1). As reflected above, the plain language in Tenn. Code Ann. § 9-8-307(a)(1)(L) waives the State sovereign immunity for contracts only for actions upon written contract by a party to the contract. Therefore, because Cadlerock cannot demonstrate that it was a party to a written contract with the State, a requirement for the Commission's exercise of jurisdiction under Tenn. Code Ann. § 9-8-307(a)(1)(L), Cadlerock's claim is not authorized by this statute.

**II. Negligent Deprivation of a Statutory Right,  
Tenn. Code Ann. § 9-8-307(a)(1)(N).**

Alternatively, Cadlerock argues that by failing to acknowledge its secured interest in the accounts receivable due Life Action under its contract with the State, the State negligently deprived it of a statutory right created under Article 9 of the UCC. The statute conferring jurisdiction in the Commission over such claims, Tenn. Code Ann. § 9-8-307(a)(1)(N) authorizes suits for:

(N) Negligent deprivation of statutory rights created under Tennessee law, except for actions arising out of claims over which the civil service commission has jurisdiction. The claimant must prove under this subdivision (a)(1)(N) that the general assembly expressly conferred a private right of action in favor of the claimant against the state for the state's violation of the particular statute's provisions[.]

Tenn. Code Ann. § 9-8-307(a)(1)(N). Cadlerock must therefore point to express language in the statute that confers a private right of action in its favor. *Draper v. State*, 2003 WL 22092544, \*3 (Tenn.Ct.App. 2003)(citing *Tate v. State*, 2003 WL 21026939 (Tenn. Ct.App. Apr 14, 2003); *A'la v. State*, 2002 WL 1838162 (Tenn.Ct.App. Aug. 13, 2002); and *Taylor v. State*, 2001 WL 873470 (Tenn.Ct.App. July 31, 2001)).

Cadlerock cites Tenn. Code Ann. § 47-9-607, which it argues permits a secured party to collect a defaulted debt by notifying an "account debtor or other person obligated on the collateral" to make payment to the secured party. Tenn. Code Ann. § 47-9-607(a)(1). That the statute requires an account debtor to make payment to a secured party on a defaulted debt, however, is not the issue for purposes of deciding if the Commission has jurisdiction under Tenn. Code Ann. § 9-8-307(a)(1)(N). The question that must be decided is whether the statute contains express language

authorizing Cadlerock to sue the State for its violation. To that end, Tenn. Code Ann. § 47-9-607(a)(3), relative to collection and enforcement after default, provides that a secured party:

may enforce the obligations of an account debtor or other person obligated on collateral and exercise the rights of the debtor with respect to the obligation of the account debtor or other person obligated on collateral to make payment or otherwise render performance to the debtor, and with respect to any property that secures the obligations of the account debtor or other person obligated on the collateral[.]

Tenn. Code Ann. § 47-9-607(a)(3).

The UCC gives a secured party certain rights and remedies with respect to enforcing a debtor's obligations subsequent to default, including the right to sue. Tenn. Code Ann. § 47-1-305(b) provides:

(b) Any right or obligation declared by this chapter and chapters 2-9 of this title is enforceable by action unless the provision declaring it specifies a different and limited effect.

Tenn. Code Ann. § 47-1-305. There is no language in the UCC explicitly stating that suit may be brought against the *State* for the statute's breach.

It is not disputed, however, that Tenn. Code Ann. § 47-1-201(27) defines "person" to include government and governmental subdivisions.

In *Byrd v. State*, 150 S.W.3d 414, (Tenn. Ct. App. 2004), the Tennessee Court of Appeals considered whether the Claims Commission had jurisdiction under Tenn. Code Ann. § 9-8-307(a)(1)(N) over claims for malicious harassment under the Tennessee Human Rights Act, which also contained no explicit reference to the State's liability in suit for its violation. There, the Court reasoned, however, that since the State is considered a "person" under the Human Rights Act, and since that Act expressly grants a right of action against such a "person" for malicious harassment, the State could be sued under Tenn. Code Ann. § 9-8-307(a)(1)(N). *Id.* at 420-421.

Employing the *Byrd* Court's reasoning here, since the UCC defines the State as a "person" subject to its provisions, and since it clearly authorizes the enforcement of rights by legal action, it appears that the requirement imposed in Tenn. Code Ann. § 9-8-307(a)(1)(N), as interpreted by the Tennessee Court of Appeals, has been met.

#### **FEDERAL PREEMPTION**

Defendant also argues that Tenn. Code Ann. § 47-9-607 is preempted by the federal anti-assignment provisions in the statute and implementing

regulations governing Medicaid, 42 U.S.C. § 1396a (a)(32) and 42 C.F.R. 424.73a, insofar as the UCC would require the State to make direct payment to Cadlerock on the contract with Life Action. The statutes governing Medicaid are applicable to TennCare, Tennessee's Medicaid managed care program. As provided for under Tenn. Code Ann. § 47-9-109(c)(1), Chapter 9 of Title 47 does not apply to the extent that "a statute, regulation, or treaty of the United States preempts" it.

Under 42 U.S.C. § 1396a (a), which contains the requirements for state plans for medical assistance, a state plan must:

*(32) provide that no payment under the plan for any care or service provided to an individual shall be made to anyone other than such individual or the person or institution providing such care or service, under an assignment or power of attorney or otherwise; except that --*

*(A) in the case of any care or service provided by a physician, dentist, or other individual practitioner, such payment may be made (i) to the employer of such physician, dentist, or other practitioner if such physician, dentist, or practitioner is required as a condition of his employment to turn over his fee for such care or service to his employer, or (ii) (where the care or service was provided in a hospital, clinic, or other facility) to the facility in which the care or service was provided if there is a contractual arrangement between such physician, dentist, or practitioner and such facility under which such facility submits the bill for such care or service;*

(B) nothing in this paragraph shall be construed (i) to prevent the making of such a payment in accordance with an assignment from the person or institution providing the care or service involved if such assignment is made to a governmental agency or entity or is established by or pursuant to the order of a court of competent jurisdiction, or (ii) to preclude an agent of such person or institution from receiving any such payment if (but only if) such agent does so pursuant to an agency agreement under which the compensation to be paid to the agent for his services for or in connection with the billing or collection of payments due such person or institution under the plan is unrelated (directly or indirectly) to the amount of such payments or the billings therefor, and is not dependent upon the actual collection of any such payment; . . .

42 U.S.C.A. § 1396a (a)(32). Because Cadlerock is a creditor, not a provider, the State argues, payment of the receivables from the contract with Life Action to Cadlerock would violate the federal law and is therefore subject to preemption.

The preemption doctrine is based on the Supremacy Clause of the United States Constitution, which provides in relevant part that the law of the United States “shall be the supreme law of the land ... anything in the constitution or laws of any state to the contrary notwithstanding.” U.S. Const. art. VI, cl. 2. State or local law that conflicts with federal law is “without effect.” *Cipollone v. Liggett Group, Inc.*, 505 U.S. 504, 112 S.Ct. 2608, 2617, 120 L.Ed.2d 407, 422 (1992).

State law preemption may be of three types: express preemption, which occurs when a statute expressly defines the scope of its preemptive effect, *Morales v. Trans World Airlines, Inc.*, 504 U.S. 374 (1992); field preemption, which occurs when a pervasive scheme of federal regulation makes it reasonable to infer that Congress intended exclusive federal regulation of the area, *Gade v. National Solid Wastes Management Ass'n*, 505 U. S. 88 (1992); and conflict preemption, which occurs when it is impossible to comply with both federal and state law or when state law stands as an obstacle to the accomplishment of Congress's purposes and objectives. *Hillsborough County, Automated Med. Lab., Inc.*, 471 U.S. 707 (1985).

As Cadlerock notes, the State's argument that federal law prohibits it from complying with Tenn. Code Ann. § 47-9-607, raises a claim of conflict preemption. Because 42 U.S.C. §1396a (a)(32) prohibits payments under a state plan for medical assistance to non-providers such as Cadlerock, the State contends that it cannot be a person obligated on collateral within the meaning of Tenn. Code Ann. § 47-9-607(a)(1), which would require that it do exactly that.

Cadlerock argues that the federal statute and regulations do not conflict with § 47-9-607, since they do not prohibit the State from paying its claim, but rather provide that the state plan must prohibit payment to entities other than the provider.

It is not disputed that Cadlerock is not a provider within the meaning of the federal Medicaid law. Moreover, the basis of Cadlerock's claim is its security interest in the accounts receivable of a TennCare provider relative to a TennCare provider agreement. There is no question but that the payment that it claims was wrongfully withheld it by the State was that which was due Life Care under its provider agreement with the State.

Cadlerock also argues that enforcement of Tenn. Code Ann. § 47-9-607 would not interfere with Congressional intent, which was not aimed at security interests like Cadlerock's. As Cadlerock suggests, the legislative history makes clear that Congress' principal concern was that the practice of "factoring" Medicare and Medicaid receivables, which were sold to collection agencies or other factoring entities for a percentage of their face

value. Claims for payment on the receivable were then submitted to the states, which Congress found were often incorrect and inflated.

*See Danvers Pathology Associates, Inc. v. Atkins*, 757 F.2d 427, 430 (1<sup>st</sup> Cir. 1985)(quoting H.R. Rep. No. 393, 95<sup>th</sup> cong., 1<sup>st</sup> Sess. 48, reprinted in 1977 U.S. Code Cong. & Ad. News 3039, 3051). The solution to this problem was to prohibit payment to non-providers.

The nature of the original security interest held by the Bank of Nashville in Life Action's receivables appears to have been merely collateral for a loan. Although the bank's interest was subsequently reassigned to Cadlerock, the nature of this transaction is not clear. However, as noted earlier, it is clear that Cadlerock is not a provider and that the 42 U.S.C. §1396a (a)(32) explicitly bars direct payment to non-providers. *See DFS Secured Healthcare Receivables Trust v. Caregivers Great Lakes, Inc.*, 384 F.3d 338, 350 (7th Cir. 2004).

This does not mean that Cadlerock was without remedy with respect to its security interest and a number of courts have recognized that Medicare and Medicaid reimbursement may be properly used as collateral for a loan. *Matter of Missionary Baptist Foundation*, 796 F.2d 752 (5th Cir.

1986)(finding that debtor's use of Medicaid reimbursement payments as collateral for a loan does not violate 42 U.S.C. 1396a(a)(32).); *Credit Recovery Systems, LLC v. Heike*, 158 F.Supp.2d at 693 ("[N]either the Medicare nor Medicaid statutes expressly proscribe a provider's assignment of the general right to receive Medicare or Medicaid receivables to a nonprovider.").

The fact, however, that Medicare or Medicaid receivables may be used as collateral does not mean that a lender can obtain payment directly using the non-judicial collection procedures outlined in Tenn. Code Ann. § 47-9-607. The Medicaid and Medicare statutes and regulations only permit direct payments to an assignee of receivables when assignments are established by, pursuant to, or in accordance with, a proper court order. *Credit Recovery Systems, LLC v. Heike*, 158 F.Supp.2d at 694; 42 U.S.C. § 1396a (a)(32)(B); *See also* Not So Perfect: the Disconnect Between Medicare and the Uniform Commercial Code Regarding Health-Care-Insurance Receivables, 9 N.C. Banking Inst. 373 (2005)("[I]f Medicare health-care-insurance receivables comprise collateral for a loan and the debtor defaults, the normal UCC remedies, such as receiving Medicare payments

directly, are not available to a secured lender. In the event of debtor default, the secured lender must resort to the judicial remedy provided in the Medicare statutes in order to obtain assignment of Medicare payments.”). As one commentator has explained:

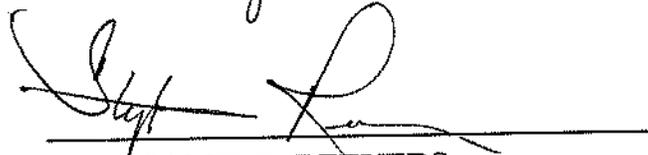
In the traditional structure, after default by the borrower, the accounts receivable may be assigned to the lender under the UCC “self-help” provisions, and the terms of the loan documents and the lender may then may collect receivables directly from the account debtors. The anti-assignment provision specifically disallows the assignment of Medicaid receivables to a lender, so they cannot be assigned to the lender automatically. For such an assignment to occur, a lender must obtain a court order for the assignment of the receivables to the lender. Once the lender receives such an order, it may then directly collect any Medicaid receivables.

Can Medicaid Receivables Secure a Credit Facility?, 121 Banking L.J. 842, 845.

Cadlerock, however, does not allege that it has sought or obtained a judicial order relative to its secured interest in Life Action’s receivables enforcement. The Commission concludes that because federal law prohibited the State from making direct payment to Cadlerock of Life Action’s Medicaid accounts receivable under the procedures outlined in Tenn. Code Ann. § 47-9-607 and because there has been no showing that

Cadlerock has obtained a court order relative to its rights to such proceeds, it has not stated a claim for negligent deprivation of statutory rights within this Commission's jurisdiction. Therefore, the motion to dismiss is granted.

It is so ORDERED this 3<sup>rd</sup> day of August, 2009.



STEPHANIE R. REEVERS  
Claims Commissioner

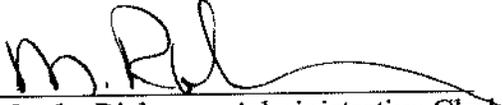
**CERTIFICATE OF SERVICE**

I hereby certify that a true and exact copy of the foregoing document has been served upon the following parties of record:

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This 4 of Aug, 2009.

  
Marsha Richeson, Administrative Clerk  
Tennessee Claims Commission