

**IN THE UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF VIRGINIA
ABINGDON DIVISION**

ABINGDON PEDIATRICS, P.C.,)	
Plaintiff)	Case No. 1:98CV00177
)	
v.)	<u>FINDINGS OF FACT</u>
)	<u>AND CONCLUSIONS OF LAW</u>
MICHAEL H. CARTER, et al.,)	
Defendants)	By: Pamela Meade Sargent
)	United States Magistrate Judge

In this case, the plaintiff, Abingdon Pediatrics, P.C., ("Abingdon Pediatrics"), asks the court, sitting in equity, to find that the defendant, Mountain Empire Business Services, Inc., ("MEBS"), has breached fiduciary duties of good faith, honest dealing and accounting owed to the plaintiff under an agreement to collect the plaintiff's accounts receivable. The plaintiff further alleges that the defendant, through its agents or representatives, has converted the plaintiff's monies for its own use.

This case was originally filed in Washington County, Virginia, Circuit Court. The case was subsequently removed to the United States Bankruptcy Court for the Western District of Virginia, based on the bankruptcy filings of two co-defendants. By order entered October 23, 1998, the district court withdrew its reference of the case to the bankruptcy court. Based on the consent of the parties, the case was transferred to the undersigned by order entered January 4, 2000.

Prior to trial, all claims against Appalachian Transmittal Services, Inc., and its owner, Sheila Stoots, were settled and the claims against these defendants were

dismissed. Also, Michael H. Carter has filed for bankruptcy, staying any claims against him. Thus, the only defendant remaining before the court is MEBS.

A bench trial was held before the undersigned on February 11-12, 2002. Based on the evidence presented, the undersigned finds that MEBS, through its agents, violated the fiduciary duties it owed to Abingdon Pediatrics and, as a result, judgment will be awarded in favor of the plaintiff in the amount of \$42,428.68.

SUMMARY OF EVIDENCE

Abingdon Pediatrics operated a pediatric medical practice in Abingdon from 1992 to 1996. Dr. James Douglas Gardner, M.D., a pediatrician, was the sole stockholder and the sole director of Abingdon Pediatrics. Over the years, Abingdon Pediatrics employed a number of physicians. Dr. Gardner's wife, Amy Gardner, a certified public accountant, performed accounting work for Abingdon Pediatrics. Mrs. Gardner also was an officer of the corporation. Mrs. Gardner testified that she was the representative of Abingdon Pediatrics most knowledgeable about the practice's accounts receivable and its computerized billing program and practices. According to Dr. Gardner, the practice averaged about \$350,000.00 a year in gross billings. Abingdon Pediatrics ceased seeing patients in November 1996 when Dr. Gardner joined a practice in Winston-Salem, North Carolina.

In the fall of 1996, Dr. Gardner and his wife spoke with W. H. Carter, ("W.H. Carter"), and his, son, Michael H. Carter, ("Carter"), about contracting with MEBS to perform Abingdon Pediatrics' patient billings after the practice closed. According to

W. H. Carter, MEBS was formed in 1992 to perform patient billing for medical and dental practices. W. H. Carter was then, and is currently, the president of MEBS. W. H. Carter testified that MEBS is not now, and never has been, set up to handle collections work involving litigation or the filing of Medicaid or insurance claims.

W. H. Carter testified that, at this meeting in the fall of 1996, he told the Gardners that, if they reached an agreement, his son, Michael Carter, would be handling the account for MEBS. W. H. Carter testified that Carter was not then, and never has been, an employee of MEBS. Rather, W. H. Carter stated that Carter was an employee of his own business, Cornerstone Marketing Group, ("CMG"). W. H. Carter testified that MEBS had subcontracted with CMG to actually process the patient billings it was obligated to perform under its contracts. W. H. Carter further testified that all of MEBS's work was performed by Carter or under Carter's direction. To the contrary, Carter testified that CMG did not have any relationship with MEBS. Instead, Carter testified that he worked for MEBS and that CMG was a separate unrelated business entity, which he owned and operated.

On January 6, 1997, Abingdon Pediatrics, through Dr. Gardner, and MEBS, through Carter, entered into a "Business Management Agreement," ("the Contract"). (Plaintiff's Exhibit No. 1.) Carter testified that he signed this contract as an agent of MEBS. W. H. Carter testified that Carter never had actual authority to enter into this or any contract on behalf of MEBS, but he admitted that Carter appeared to have the authority to do so based on his comments to the Gardners. W. H. Carter also admitted that he later learned that Carter was performing work for Abingdon Pediatrics on behalf of MEBS, but he claimed that he never actually saw the Contract until only a few

months before trial. W. H. Carter also admitted that, prior to his statements at trial, he had never informed the Gardners that Carter did not have authority to act on behalf of MEBS.

Under MEBS's Contract with Abingdon Pediatrics, MEBS and its "Associates" were obligated to perform the following services:

- A. A monthly service that would include, processing incoming mail payments, posting such payments to relative accounts, making deposits to designated bank accounts, and in general making any computer transactions required to maintain account activities.
- B. To process and procure payments on the listed "Bad Debt Accounts", accounts currently over 150 days....

In exchange for these services, Abingdon Pediatrics agreed to pay MEBS a flat fee of two percent of all of its accounts receivable within the 0- to 150-day time frame. The parties further agreed that these accounts receivable totaled \$76,830.53 on January 6, 1997.¹ Abingdon Pediatrics also agreed to pay MEBS 50 cents per invoice/statement sent on the first day of February, March, April and May 1997. Abingdon Pediatrics also agreed to pay for the costs of these invoices/statements and any associated mailing costs. W. H. Carter has admitted that Abingdon Pediatrics paid MEBS the two percent flat fee it owed for performing billing services on its current accounts receivable. Mrs.

¹The evidence in this case, (Docket Item No. 55, Plaintiff's Exhibit No. 3), shows that the amount of accounts receivable in the 0- to 150-day time frame actually totaled \$59,939.64 on January 6, 1997. The parties apparently agreed to the higher figure of \$76,830.53 from a December 31, 1996, report for purposes of setting MEBS's two percent fee under the Contract.

Gardner testified, however, that Abingdon Pediatrics paid MEBS approximately \$3,000.00, while two percent of \$76,830.53 would total only \$1,536.61.

The Contract further states:

5. As accounts time into the 150+ day category, a collection process ... will begin ... pursuant to Section 8.01-13 of the 1950 Code of Virginia, as amended.
6. Starting in January 1997, all accounts in the 150+ category will be processed by MEBS and [its] assigned associates to start a collection process. The fee for the 150+ day accounts will be 35% on collected funds. By this agreement, Abingdon Pediatrics, P.C., assigns MEBS and [its] associates full rights to collect on [its] behalf to the full extent of the law.

The Contract also states that MEBS would bill Abingdon Pediatrics on a monthly basis for its processing fees and expenses associated with mailing invoices on all current accounts receivable. The Contract further states that Abingdon Pediatrics would provide its computer and computerized billing system to MEBS for use in collecting and tracking its accounts receivable.

Both Dr. Gardner and Mrs. Gardner testified that this collection of accounts more than 150 days old was a significant portion of MEBS's obligation under the Contract. Mrs. Gardner explained that this obligation was significant because only a small portion of the amounts owed to Abingdon Pediatrics was in the 0-150 day range. Mrs. Gardner also testified that she was told that MEBS would pursue these collections through filing suit against the responsible parties, if necessary. It is undisputed that MEBS never filed any such suits.

Carter testified that, prior to entering into the Contract with Abingdon Pediatrics, he, on behalf of MEBS, had entered into an agreement with Appalachian Transmittal Services, Inc., ("ATS"), a company owned and operated by Sheila Stoots, for ATS to perform many of MEBS's obligations under the Contract. In fact, Carter stated that Stoots accompanied him when he picked up the computer and computerized billing system from Abingdon Pediatrics' Abingdon office in January 1997.

Mrs. Gardner testified that Abingdon Pediatrics used the Medic computer billing and accounting software. According to Mrs. Gardner this software showed that Abingdon Pediatrics' accounts receivable totaled \$262,212.45 when MEBS took over its patient billing in January 1997. (Plaintiff's Exhibit No. 3.) This amount included \$73,857.57 owed by various insurance companies on pending insurance claims and \$188,354.88 owed by patients. Mrs. Gardner testified that all amounts owed Abingdon Pediatrics when its accounts were turned over to MEBS were reflected on the Medic system in either the pending insurance category or the accounts receivable categories.

Stoots and Carter assert that Abingdon Pediatrics' computerized billing system showed that its accounts receivable totaled only \$188,354.88 as of January 6, 1997. Of this amount, \$128,415.24 was in the 150+ day category as of January 6, 1997. Carter testified that he is not sure what the category listed as "insurance pending" meant, but he did not believe it showed additional amounts owed to Abingdon Pediatrics. A Medic report dated August 1998, however, clearly shows that there were amounts due in the insurance pending category that were not reflected in the total balance due from the patients. (Plaintiff's Exhibit No. 2.)

In January 1997, Abingdon Pediatrics gave Carter a key to its Abingdon post office box, and Carter began to pick up patients' payments from that box and either post them to the computerized billing system and deposit them or give them to Stoots to post and deposit. From January to August 19, 1997, all payments received were deposited into Abingdon Pediatrics' Nationsbank account, according to Carter. After August 19, 1997, all payments, with the exception of certain insurance and Medicaid payments, were deposited into ATS's so-called "Collections Accounts." The Gardners deny ever authorizing the depositing of Abingdon Pediatrics' funds into an ATS bank account. Nevertheless, the evidence shows that from August 19, 1997, to September 14, 1997, these deposits were made into an ATS account at Premier Bank in Lebanon. Beginning September 15, 1997, these deposits were made into an ATS account at First Bank & Trust in Lebanon.

Stoots has admitted that Abingdon Pediatrics' funds were commingled in these accounts with funds from ATS's other clients and that she did not keep any ledger to distinguish the funds of one client from another. Stoots also has admitted that she used these Collections Accounts as ATS's general operating accounts. Stoots was the only person authorized to write checks on either of these Collections Accounts. Stoots also has admitted that, on occasion, she used funds paid into these accounts and held on Abingdon Pediatrics' behalf to pay ATS's operating expenses.

The evidence also shows that Stoots and ATS did not turn over Abingdon Pediatrics' share of these payments in a timely manner. (Plaintiff's Exhibit No. 11.) In fact, when payments of Abingdon Pediatrics' share of these collections were finally made, at least three of ATS's checks to Abingdon Pediatrics' were returned due to

insufficient funds in its account. (Plaintiff's Exhibit No. 14.) Furthermore, Stoots and Carter have admitted that bank statements for ATS's Collection Accounts show that there was often less money in these accounts than was owed to Abingdon Pediatrics at the time. (Plaintiff's Exhibit No. 12.) Stoots also testified that MEBS, through Carter, knew and approved of all of her actions in handling the Abingdon Pediatrics' accounts receivable. Also, Mrs. Gardner testified that when she questioned Carter with regard to Stoots's failure to turn over Abingdon Pediatrics' share of the collections account, Carter told her that Stoots was trying to build up the balance in ATS's bank account so that ATS could qualify for a Small Business Administration loan.

The parties have stipulated that, after MEBS began processing Abingdon Pediatrics bills and payments, \$51,061.90 in cash and insurance proceeds were deposited into Abingdon Pediatrics' Nationsbank account. In an accounting filed with the court, (Docket Item No. 55), ("the Accounting"), Carter and Stoots have admitted that ATS collected \$38,763.01 prior to March 1998 from Abingdon Pediatrics' accounts receivable which were more than 150 days old. Based on the Contract, Abingdon Pediatrics should have received 65 percent of this amount or \$25,195.96. Instead, ATS paid Abingdon Pediatrics only \$18,643.32, leaving \$6,552.64 still owed to Abingdon Pediatrics.²

Stoots and Carter also claim that ATS entered into a separate agreement with Abingdon Pediatrics on February 1, 1997, to file unfiled insurance and Medicaid claims. Carter testified that MEBS had nothing to do with this separate agreement and

²This court previously entered partial summary judgment in favor of Abingdon Pediatrics for this amount.

that MEBS did not agree to perform this service. Carter further testified that MEBS was not equipped to file insurance claims on behalf of its clients and that MEBS was not supposed to get any fee for providing this service to Abingdon Pediatrics.

Carter admitted, however, that he had drafted a document entitled MEBS/ATS Project. This documents states:

Proposal for payments and expenses.

1. Approximate rate of \$10.00/hr for filing, key punch, and associated paperwork.
2. Regular A/R statement process. (01-149 days)
A cost basis is in force and includes all associated costs to be handled by Abingdon Pediatrics, such as paper, ribbon, statements and postage.
A .50 cent per statement charge is also in effect.
3. "Bad Debt" category. (150+ days)
35% cost of recovery in this category (20% ATS, 15% MEBS)
A \$2.50 fee will be assessed on each insurance claim requiring filing.
(with consideration to overall costs)
4. Any insurance on file in A/R that has not been filed with insurance company or is in process of being re-filed. (A \$2.50/claim charge is in effect)
5. "Free Money" category. This category includes any insurance claim or Medicare claim that is listed on A/R but is currently not filed (UN).
All claims in this category will be filed to determine acceptance or rejection
 - a. A \$2.50 per claim charge will be totaled.
 - b. Any patients that end up with a credit balance will be given credit balance with a \$10.00 filing fee and associated per claim fee, based

on total number of claims relative to total number of patients receiving credit payments.

(Plaintiff's Exhibit No. 17.) Carter testified that he drafted this document some time in the summer of 1997 based on his ongoing conversations with Mrs. Gardner.

While Stoots, in her responsive pleading, had asserted that she had entered into a written contract with Dr. Gardner to file certain insurance claims, Stoots testified that the parties reached an oral agreement at a February 1, 1997, meeting. Stoots claims that at this meeting she informed Dr. and Mrs. Gardner that she and Carter had discovered a number of unfiled insurance claims on Abingdon Pediatrics' computerized billing system. Stoots claims that she then produced a report from the Medic system showing numerous pages of unfiled insurance claims. Stoots produced a report at trial dated December 2, 1999, which she claimed contained the same information as the report she produced to the Gardners in February 1997. (Plaintiff's Exhibit No. 18.) This report indicates the date on which each of the charges listed were incurred, and none of these charges was incurred after December 1994. In fact, many of these charges were incurred in 1992 and 1993.

According to Stoots, these unfiled insurance claims totaled approximately \$645,000.00. Stoots claims that she discovered these unfiled claims when she noticed that many of the accounts on the computerized billing system contained a "UN" code. When she contacted Lorraine Challinor, Abingdon Pediatrics' office manager, Stoots claims that Challinor said that this "UN" code designated unfiled insurance claims. Stoots claims that at this February 1 meeting Dr. Gardner agreed to allow ATS to begin filing these unfiled claims with private insurance companies and Medicaid. Stoots also

claims that Dr. Gardner agreed that Abingdon Pediatrics would pay ATS \$2.50 for each primary insurance claim filed and \$1.50 for each insurance claim which was refiled. Stoots also asserts that Dr. Gardner agreed that ATS's fees for these filings would come out of any proceeds generated by these filings.

In support of Stoots's testimony, MEBS offered a letter to the Virginia Department of Medical Assistance Services. (Defendant's Exhibit No. 1.) This letter was signed by Dr. Gardner and was dated February 1, 1997. On its face, this letter authorized Electronic Tabulating Service, Inc., to file Medicaid claims on behalf of Dr. Gardner. MEBS also submitted a form signed by Dr. Gardner on February 1, 1997, permitting the filing of Medicare claims.³ (Defendant's Exhibit No. 1.) Stoots also produced a report at trial which she testified listed each unfiled insurance claim ATS had filed. (Defendant's Exhibit No. 2.) This report shows a total of \$645,685.65 in insurance claims. This report also shows that none of these claims were filed by Stoots prior to March 1997. Stoots also testified that, based on her experience with filing health insurance claims for other providers, she was aware at the time that she filed these claims that most health insurers would not pay a claim filed more than 18 months after the date of service.

Stoots testified that all monies recovered from these filings went into an "Insurance Recovery Account." Despite his assertion that MEBS had nothing to do with this arrangement, Carter testified that he opened this account at Premier Bank in

³The parties have offered no explanation as to why a pediatric practice would have a need to file Medicare claims. Although the court notes that, under certain circumstances, social security disability benefits recipients qualify for health care coverage under the Medicare system regardless of age.

Lebanon in the name of "MEBS/ATS; DBA: Insurance Recovery." Only Stoots and Carter were authorized to sign checks drawn on this account. Carter and Stoots both claim that they advised Dr. and Mrs. Gardner that this Insurance Recovery Account had been opened and that the Gardners had agreed to allow ATS to take proceeds out of this account as its payment for these filings. Carter also testified that he forwarded a signature card for this account to Gardners, to allow them to sign checks on this account. Mrs. Gardner denied that she had ever received this signature card. Carter also admitted that he had never provided the Gardners with any monthly bank statements for this account until after the Gardners had retained counsel. In fact, Carter stated that he had received the bank statements for this account at Abingdon Pediatrics' post office box and turned them over to Stoots, who kept them at ATS's office.

Stoots has admitted that she did not bill Abingdon Pediatrics for any charges related to these filings until after this case was commenced.

Carter testified that the amounts received as a result of these filings were not posted on Abingdon Pediatrics' computerized billing system. Therefore, Carter has admitted that he does not know what, if any, of these sums were owed to Abingdon Pediatrics. Both Stoots and Carter have admitted that some of these insurance filings were for Abingdon Pediatrics' patients who had paid Abingdon Pediatrics in full, and, therefore, any money recovered by these filings would be owed to the patient, not Abingdon Pediatrics. Neither has provided any information showing the number of such claims filed for which no amounts were owed to Abingdon Pediatrics. Stoots admitted, however, that she did not have the permission of any patients to file any claims on their behalf. MEBS submitted one Explanation of Benefits form, (Defendant's Exhibit No.

3), and Abingdon Pediatrics submitted several Explanation of Benefits forms generated by these insurance claims and produced by Stoots at trial, (Plaintiff's Exhibit No. 19). Each of these forms showed that these particular claims had been filed with the health insurer previously and were, therefore, denied.

The evidence presented to the court also shows that on at least two occasions, Stoots filed insurance claims in excess of any amount owed by the patient to Abingdon Pediatrics. A January 6, 1997, Medic report lists a number of patients and/or responsible parties, and it shows the amounts owed on their accounts. (Plaintiff's Exhibit No. 3.) This document shows that, as of January 6, 1997, Carl Tittle, Jr. owed \$221.00 on account number 12897 and Steve Wann owed \$198.00 on account number 12912. Stoots's own documentation, however, shows that in April 1997 she filed a total of \$229.00 in insurance claims against Tittle's insurer, Charter Benefits, and a total of \$218.00 in claims against Wann's insurer, John Hancock. (Defendant's Exhibit No. 2.) This documentation does not show that ATS ever received any payment on these claims. Furthermore, Stoots produced a list, which she generated using the Medic system, and which she stated showed all insurance claims that were unfiled when MEBS began handling Abingdon Pediatrics' accounts in January 1997. (Plaintiff's Exhibit No. 18.) This list shows that Tittle had only \$193.00 in charges incurred on account number 12897 and Wann had only \$150.00 in charges incurred on 12912. All of these charges were incurred for services performed in 1994.

These documents also show that these purported unfiled insurance claims listed some services for which Abingdon Pediatrics was not owed any amount. For instance, the Medic report shows that, as of January 6, 1997, Tommy Caudell owed only \$87.00

on account number 10756; \$18.64 on account number 10281 and \$123.90 on account number 10135. The list of purported unfiled insurance claims, however, shows claims on account number 10756 for Christopher Caudell totaling \$195.50 for services rendered in 1993 and 1994, claims on account number 10281 for Nicholas Caudell totaling \$157.00 for services rendered in 1993 and claims on account number 10135 for Bradley Caudell totaling \$230.00 for services rendered in 1993. Each of these amounts exceeds the amount owed to Abingdon Pediatrics on these accounts as of January 6, 1997.

The Medic report also shows that, as of January 6, 1997, Brian Smith owed \$67.00 on account number 10051; Linda Dolly owed \$108.00 on account number 10684; Larry Rouse owed \$32.40 on account number 13552; Sherry Cook owed \$96.00 on account number 14071 and \$107.20 on account number 14072; Tim Groseclose owed \$46.40 on account number 10222; and Tommy Nicholas owed \$443.00 on account number 10426. The list of purported unfiled insurance claims, however, shows claims on account number 10051 for Joseph Smith totaling \$164.00 for services rendered in 1994; claims on account number 10684 for Brian Dolly totaling \$154.00 for services rendered from 1992 to 1994; claims on account number 13552 for Travis Wynegar totaling \$45.00 for services rendered in 1994; claims on account number 14071 for Alicia Cook totaling \$120.00 for services rendered in 1994; claims on account number 14072 for Derrell Cook totaling \$134.00 for services rendered in 1994; claims on account number 10222 for Kristin Groseclose totaling \$235.00 for services rendered in 1992 and 1993; and claims on account number 10426 for Jonathan Nicholas totaling \$509.00 for services rendered in 1992-94. Again, each of the

amounts listed as unfiled insurance claims for these accounts exceeds the amount owed to Abingdon Pediatrics on the account as of January 6, 1997.

Stoots also produced an example of a patient account statement generated by the Medic system, which purported to support her claim that there were numerous unfiled insurance claims listed on the Medic system. (Defendant's Exhibit No. 5.) This statement was dated February 26, 1997. While this statement listed "UN" by four separate charges incurred from 1992 to 1994, the statement on its face also indicated that there was no outstanding balance owed to Abingdon Pediatrics on this patient's account. Furthermore, the statement also indicated that insurance payments on this account had been received as recently as January 2, 1997. Despite the fact that this patient owed no balance to Abingdon Pediatrics, the evidence produced by Stoots shows that she filed insurance claims totaling \$609.00 on behalf of this patient.

Stoots also testified that none of this approximately \$645,000 in unfiled claims was included in the \$188,354.88 listed as the total accounts receivable due from patients on Abingdon Pediatrics' computerized billing system as of January 6, 1997. There also is evidence that both Stoots and Carter referred to this \$645,000 in unfiled claims as "free money."

Both Dr. and Mrs. Gardner assert that Abingdon Pediatrics never agreed for ATS to perform any electronic filings for Abingdon Pediatrics other than filings with Medicaid. Both assert that they believed that the electronic filings with Medicaid were part of MEBS's obligations under the Contract. Dr. Gardner has admitted that he signed a document at this February 1 meeting to allow ATS to file Medicaid claims

electronically on Abingdon Pediatrics' behalf. (Defendant's Exhibit No. 1.) Both assert that they believed that the patient, and not Abingdon Pediatrics, would be responsible to pay the \$2.50 filing fee for each claim electronically filed with a private insurance carrier. Both also assert that they had no knowledge of the establishment of this "Insurance Recovery Account" and that they had never authorized Stoots or Carter to make any disbursements from this account. Both testified that it would not have been possible for there to have been \$645,000.00 in unfiled insurance claims when Abingdon Pediatrics turned over its accounts receivable to MEBS. In fact, Mrs. Gardner testified that it would take a physician, who saw an average of 30 patients a day, approximately two and one-half years to generate this amount in insurance claims. Dr. Gardner testified that it would take two physicians, who worked full-time, a full year to generate this amount in fees.

In the Accounting, Stoots and Carter assert that \$19,369.96 was received as a result of these insurance filings and deposited into the Insurance Recovery Account. Documents attached to the Accounting show, however, that \$25,339.12 was disbursed from this account through checks drawn on the account or debit memos. Regardless of the amount, Stoots and Carter admit that, other than a few patient refunds, all funds paid into this Insurance Recovery Account were paid out to either ATS or CMG or on their behalf. Both also admit that none of these disbursements were reported to either Dr. or Mrs. Gardner when they were made. Carter testified that none of the money in this Insurance Recovery Account was paid directly to MEBS.

Stoots admitted that she wrote several checks from this account to Carter's business, CMG. Stoots said that these checks were for amounts owed to CMG by

ATS. Stoots explained that CMG had advanced ATS \$1.98 for each insurance claim that she had filed for Abingdon Pediatrics' patients. Carter testified that CMG had advanced Stoots \$20,000, of which she repaid only \$13,000 prior to filing bankruptcy.

Mrs. Gardner testified that she did not learn of the existence of this separate Insurance Recovery Account until sometime in 1997. In June 1997, Mrs. Gardner received two letters from Carter which mentioned MEBS's and ATS's effort to collect what Stoots and Carter believed were unfiled insurance claims. (Plaintiff's Exhibit Nos. 6 and 7.) In one undated letter, Carter, on behalf of MEBS, stated:

To date 12,779 claims, listed as un-filed on your system have been submitted to the proper insurance companies. Approximately 2000+ claims have been sent back. Monies recovered in this category goes into a Insurance Recovery account to await final totals. As of 5/8/97, \$11,000+ has been brought in.

The 12,779 claims, (20773 transactions), represent approximately \$640,000 in "possible" revenues, however, it is reasonable to assume that only a portion will actually pay out....

...The actual collection process is now starting this activity will probably go through the next two or more months depending on additional efforts required to get judgments.

(Plaintiff's Exhibit No. 6.) This letter from Carter makes no mention of any disbursements from this account.

Carter testified that the 12,779 claims filed by Stoots were not all of the unfiled claims listed on the Medic system. In particular, Carter stated that Stoots simply

stopped filing these claims until it could be determined whether any insurance payments would be made on the claims already filed.

In response to this letter, Mrs. Gardner said that she spoke to Carter and told him that it was not possible for there to have been \$645,000 in unfiled insurance claims on the Medic system. Mrs. Gardner made notations concerning her comments on this letter. Mrs. Gardner testified that Carter called this "free money." She stated that Carter told her that there would be no expense to Abingdon Pediatrics for these filings. Instead, Carter stated that if the patient was due a refund from these insurance payments, the patient should be willing to pay the \$2.50 filing fee. Mrs. Gardner also testified that Carter told her that any amounts paid into this Insurance Recovery Account would be held and not paid out until all amounts were received.

In a letter dated June 9, 1997, Carter, this time on behalf of MEBS and ATS, stated the following:

3. Insurance Recovery is still proceeding. Approximately \$640,000 was on system as "un-filed".... As you know, there will be a min. charge of \$2.50 to the patient for refiling. If the recovery amount reaches a higher level than the projected \$100,000 it would be possible to attach a fee structure for processing and refiling that is fair and equitable to us in efforts given.

(Plaintiff's Exhibit No. 7.) Again, this June 9 letter makes no mention of any disbursements from the Insurance Recovery Account. Documents submitted into evidence, however, show that approximately \$12,000.00 had disbursed from this account to CMG, Carter, ATS or Stoots by June 9, 1997. (Plaintiff's Exhibit No. 5.)

The evidence presented also includes a September 17, 1997, letter from Mrs. Gardner to Stoots seeking information regarding ATS's role in performance of MEBS's obligations under the Contract. (Plaintiff's Exhibit No. 8.) In this letter, Mrs. Gardner asked Stoots to answer the following questions:

1. Define the service you have been contracted to do for Abingdon Pediatrics, P.C.
2. How many accounts are you depositing money into? List bank and account numbers.
3. List all activity in the account where the "Free Money" as [Carter] called it, [is deposited], such as all deposits and all disbursements.
4. The money that has been collected since the collection letter went out. I need the date and amount of each deposit.

This letter also stated, "... I did not know that numerous bank accounts were to be used to deposit Abingdon Pediatrics' monies, please explain this to me."

Carter, not Stoots, provided a written response to Mrs. Gardner's inquiries, (Plaintiff's Exhibit No. 9), which included the following statements:

#1 ATS was contracted by MEBS to electronically file any ... outstanding insurance claims that were listed as unfiled or pending, and upon the last statement run to proceed with a collection process on any outstanding balances.

#2	A.	Abingdon Pediatrics	Nations
		Regular banking account	
	B.	MEBS/ATS/Abingdon Pediatrics	Premier Bank/Lebanon
		Insurance Recovery account	
	C.	ATS Collection account	Premier Bank/Lebanon

ATS account used as clearing/holding account for checks received in collections

#3 "FREE MONEY"

Upon initial review of the Abingdon Pediatrics [accounts receivables] it was noted that a large no. of insurance claims were either listed as "Pending" or "Unfiled". It was thought that due to either a large backlog of paperwork not filed OR lack of any accounting function, that insurance claims were not being handled properly and it appeared, by review of accounts, that people had been paying on their accounts and insurance was ignored.

MEBS along with ATS thought that if these types of claims were refiled, it would provide a large amount of receivables to provide for:

- a. Clearing of account in general
- b. Providing a payment source to offset an outstanding balance on any account
- c. The possibility of a revenue source to MEBS/Abingdon Pediatrics by virtue of charging a reasonable fee for recovery of any payoff.

As you recall with discussions with ATS, there was a general fee of \$2.50/claim to re-file or submit to any insurance company.

With the advent of this "pending & unfiled" group of accounts completely paying out, it was thought that a general overall fee of +/- 25% could reasonably be charged and this could have been probationally (sic) split between the companies to cover misc. expenses.

* It was also thought that this area could possibly cover some of the monthly costs that were chargeable (sic) to Abingdon Pediatrics for billing and operational costs per general agreement in lieu of Abingdon Pediatrics actually writing a check.

There were 12,899 claims re-filed by ATS (listed as unfiled or pending on A/R)

At \$2.50 each, the general cost for re-filing was \$32,247.50

These were processed in various batches with associated sending dates. (on computer)

There has been \$20,699.00 returned with a combination of batch payback and several account balances returned to patients. This represents 64% of costs.

In this written response, Carter also told Mrs. Gardner that Abingdon Pediatrics' computerized billing system showed that its accounts receivable total on January 6, 1997, was \$188,354.88. He also stated that the most recent report taken from the computerized billing system showed that Abingdon Pediatrics' accounts receivable total was \$121,093.97. (Plaintiff's Exhibit No. 9.)

Carter admitted that, despite Mrs. Gardner's specific inquiry, he did not inform her of the disbursements that had been made out of the insurance proceeds placed into the Insurance Recovery Account. Carter also admitted that bank records showed that \$25,970.37 was disbursed from the Insurance Recovery Account. (Plaintiff's Exhibit No. 5.) Carter further admitted that either he or Stoots signed each check or authorized each debit drawn on this account. He also admitted that he had known of each of these disbursements when he had responded to Mrs. Gardner's inquiry.

Both Mrs. Gardner and Dr. Gardner testified that Abingdon Pediatrics had never received any documentation supporting ATS's claim that it had electronically filed more than 12,000 insurance claims prior to trial. Furthermore, they testified that they had never seen any Explanation of Benefits forms from any insurance company with regard to any such electronic filings, prior to those produced by Stoots at trial. Mrs. Gardner stated that Abingdon Pediatrics' relationship with MEBS and Carter "went down hill" after she received Carter's response to her September 9, 1997, letter.

Mrs. Gardner testified that the last Medic report received from ATS was dated August 1998 and showed that Abingdon Pediatrics' outstanding accounts receivable totaled \$88,666.19 at that time. (Plaintiff's Exhibit No. 2.) Mrs. Gardner stated that this same report showed \$48,983.62 in pending insurance claims. Thus, according to Mrs. Gardner, this report showed a total of \$129,648.81 owed to Abingdon Pediatrics. Mrs. Gardner also testified that any Medicaid write-offs posted to the Medic system would have been subtracted from the pending insurance claims total, not from the patients accounts receivable total. According to this report, Mrs. Gardner stated that MEBS had posted \$132,563.64 in transactions to the Medic system while handling Abingdon Pediatrics' patient accounts. Not including the monies deposited into the Insurance Recovery Account, Mrs. Gardner stated that MEBS had accounted to Abingdon Pediatrics for only \$109,020.75 of this amount. (Plaintiff's Exhibit No. 4.) Mrs. Gardner also testified that when Abingdon Pediatrics retrieved its computer and computerized billing system from Stoots, it would not function.

Although he had previously testified to the contrary, Carter also testified that all payments received by MEBS on behalf of Abingdon Pediatrics were posted on the Medic system. Carter further testified that the difference between the beginning accounts receivable total on January 6, 1997, and the ending accounts receivable totals in August 1998 showed the total of all payments and write-offs posted by MEBS or at its direction on the Medic system.

Evidence also was presented that ATS sent out letters to Abingdon Pediatrics' patients whose accounts were older than 150 days stating:

Your account has been purchased from the original creditor, and **APPALACHIAN TRANSMITTAL SERVICES, INC. NOW OWNS YOUR ACCOUNT. PAYMENT MUST BE MADE TO US DIRECTLY, Or YOUR ACCOUNT WILL NOT BE PROPERLY CREDITED. DO NOT MAKE PAYMENT TO ABINGDON PEDIATRICS, P.C.!!!!** Please contact my office as soon as possible so we can work this matter out. Payment may be mailed to the above address....

(Plaintiff's Exhibit No. 15.) This letter was sent by S. P. Stoots, and it lists ATS's address, not Abingdon Pediatrics' address, as the address to which patients should mail payments. Mrs. Gardner testified that Abingdon Pediatrics never assigned or sold its accounts to ATS and never authorized patients' account balances to be paid to ATS. Mrs. Gardner stated that through discovery she had learned that ATS also had endorsed and deposited into its accounts several checks made out to Dr. Gardner individually.

In March 1999, this court ordered the defendants, within 30 days, to file an accounting with the court of all payments received on behalf of Abingdon Pediatrics, the date of receipt, the amount received, the patient's account for which the payment was received and identity of the payor, the disposition of the payment or any part thereof including the amount and date of distribution, the identity of the party to whom distribution was made and any bank account into which such was deposited. (Plaintiff's Exhibit No. 21.) In addition, the court ordered that, if distribution of funds had been made to anyone other than Abingdon Pediatrics, the defendants were to state the purpose of each distribution. In response to the court's order, the defendants, on September 6, 2000, filed their Supplemental Response To Plaintiffs' Discovery Pursuant To Order Entered By This Court On March 24, 1999, (Docket Item No. 55)

("the Accounting"). Although the court had ordered that this accounting be under oath, the acknowledgment attached to it reflects that neither Carter or Stoots swore to its accuracy. In this Accounting, Carter and Stoots stated that all payments received, including those deposited into the Insurance Recovery Account, were entered into the Medic system.

In this Accounting, Carter and Stoots also stated that, when they received Abingdon Pediatrics' system, a large number of unfiled insurance claims were noted on the Medic system as "pending." There is no mention of the "UN" code in the statements attached to the Accounting. The defendants incorrectly represented that only \$19,369.96 was generated through ATS's filing of "pending" insurance claims and deposited into the Insurance Recovery Account. They also incorrectly represented that only \$19,363.96 had been paid out of this account.

Through this Accounting, Carter and Stoots stated that they had received and posted to the Medic system a total of \$107,688.69 in payments. Included in this total were \$51,061.90 received from patients and insurance companies and placed in the Abingdon Pediatrics Nationsbank account, \$38,763.01 received for accounts more than 150 days old and placed in ATS's Collections Accounts and \$19,369.96 received from the filing of "pending" insurance claims and placed into the Insurance Recovery Account. Stoots and Carter acknowledged that these amounts totaled \$1,506.18 more than the amounts that they claim that they had entered into the Medic system.

Attached to the Accounting is a list of all payments received from collections -- the accounts more than 150 days old. This list shows that ATS received payments on these accounts from August 1997 through March 1998.

ANALYSIS

As stated above, Abingdon Pediatrics filed this suit in equity requesting that the court order MEBS to provide a full and complete accounting of all amounts it or its agents received on Abingdon Pediatrics' behalf and to pay all such amounts over to Abingdon Pediatrics. Abingdon Pediatrics also asks the court to find that MEBS has forfeited any fees paid to it based on MEBS's breach of its fiduciary duties of good faith, honest dealing and accounting.

Although the court's jurisdiction over this case stems out of its bankruptcy jurisdiction, the issues to be resolved are not issues of federal law. That being the case, this court should apply the conflicts rules of the forum state, Virginia, in determining which state's law should control. *See Merritt Dredging Company, Inc., v. Campbell*, 839 F.2d 203, 205-06 (4th Cir. 1988). Under Virginia's choice of law rules, a tort claim, including a claim for breach of fiduciary duties, is to be governed by the law of the place of the wrong, the *lex loci delicti*. *See Airlines Reporting Corp. Pishvaian*, 155 F. Supp. 2d 659, 664 n.9 (E.D. Va. 2001) (citing *Jones. v. R.S. Jones and Assoc., Inc.*, 246 Va. 3, 5, 431 S.E.2d 33, 34 (1993); *Buchanan v. Doe*, 246 Va. 67, 71, 431 S.E.2d 289, 291 (1993)). Furthermore, Virginia law is well-settled that the place of the injury supplies the governing law in tort actions. *See Lachman v. Pennsylvania*

Greyhound Lines, Inc., 160 F.2d 496, 500 (4th Cir. 1947) (citing *C.I.T. Corp. v. Guy*, 170 Va. 16, 195 S.E. 659 (1938)). Here, the alleged breach and resulting loss occurred in Virginia. Therefore, I hold that Virginia law controls the substantive legal questions at issue in this case.

Turning to the facts of this case, W. H. Carter asserted that his son, Carter, never had actual authority to enter into any contracts on behalf of MEBS. Nonetheless, he conceded that, based on his statements to the Gardners, Carter had apparent authority to do so. *See Walker v. Winchester Mem. Hosp.*, 585 F. Supp. 1328, 1330 (W.D. Va. 1984) (quoting *Wright v. Shortridge*, 194 Va. 346, 352-53, 73 S.E.2d 360, 364-65 (1952)). The evidence also establishes that, regardless of whether Carter had the actual or apparent authority to enter into the Contract, MEBS ratified his actions when W.H. Carter learned that Carter had begun performing services under the contract on behalf of MEBS and MEBS did not disavow Carter's actions. *See Coastal Pharmaceutical Co., Inc. v. Goldman*, 213 Va. 831, 839, 195 S.E.2d 848, 854 (1973) (if principal knows that an agent has transcended his authority, the principal must promptly disavow the act, or the act becomes the act of the principal). In fact, MEBS has not disavowed any of the acts of Carter or Stoots to date. Furthermore, W. H. Carter conceded that Carter had actual authority to conduct all of MEBS's business. The undisputed evidence shows that Carter, on behalf of MEBS, contracted with ATS to perform work on the Contract. Therefore, I find that MEBS is responsible for the actions of its agents, Carter, Stoots, CMG and ATS, in their handling of Abingdon Pediatrics' accounts receivable.

MEBS, through its pleadings, also has admitted that, in performance of its obligations under the Contract with Abingdon Pediatrics, MEBS and its agents, including ATS, owed Abingdon Pediatrics the fiduciary duties of good faith, honest dealing and accounting. MEBS argues, however, that the evidence presented shows that it has accounted for all amounts paid to it or its agents on behalf of Abingdon Pediatrics and that no additional amounts, other than the \$6,552.64 that the court previously awarded on grant of partial summary judgment, are owed to Abingdon Pediatrics. I disagree.

The evidence presented at trial clearly shows that MEBS, through its agents, Carter, Stoots, ATS and CMG, breached its fiduciary duties of honest dealing and accounting. While it may be argued whether their actions amounted to embezzlement, the undisputed evidence shows that Stoots, with the knowledge and approval of Carter, at the very least converted Abingdon Pediatrics' funds for her own use. *See Federal Ins. Co. v. Smith*, 144 F. Supp. 2d 507, 517-518 (E.D. Va. 2001) (quoting *Universal C.I.T. Credit Corp. v. Kaplan*, 198 Va. 67, 75-76, 92 S.E.2d 359, 365 (1956) (conversion is any distinct act of dominion wrongfully exerted over the property of another, including cash, and which is in denial of his rights or inconsistent therewith)). In particular, both Stoots and Carter have admitted that they did not promptly pay over to Abingdon Pediatrics its share of payments made on collections accounts. Instead, these amounts were placed into ATS's bank accounts and were used by Stoots to pay ATS's operating expenses. In fact, MEBS admits that it still owes Abingdon Pediatrics \$6,552.64 of these amounts.

Also, much argument has been made in this case over which party carries the burden of proof. Nonetheless, "[t]he law governing the responsibilities of fiduciaries and the burden of proof required to exonerate a fiduciary when self-dealing is involved have been well established in Virginia for a considerable period of time." *Stickley v. Stickley*, 50 Va. Cir. 526, ____, 1999 WL 1441941 at *1 (1999). When a fiduciary relationship exists, any transaction to the benefit of the fiduciary and to the detriment of the other party is presumptively fraudulent under Virginia law. *See Nicholson v. Shockey*, 192 Va. 270, 278, 64 S.E.2d 813, 817 (1951). That being the case, once a fiduciary relationship has been established and proof of fraud or self-dealing has been offered, the burden shifts to the fiduciary to establish the honesty of his actions. *See Kanawha Valley Bank v. Friend*, 162 W.Va. 925, 929, 253 S.E.2d 528, 531 (1979) (citing *Nicholson*, 192 Va. 270, 64 S.E.2d 813). Furthermore, the fiduciary has the burden to overcome the presumption of fraud by clear and satisfactory evidence, which is a higher standard than a mere preponderance of the evidence. *See Nicholson*, 192 Va. at 282, 64 S.E.2d 813, 820.

In this case, MEBS has admitted that it and its agents owed Abingdon Pediatrics certain fiduciary duties in the handling of its accounts. Also, the undisputed evidence shows that MEBS has violated those duties in that it has admitted that its agents did not turn over all monies belonging to Abingdon Pediatrics. That being the case, the burden shifts to MEBS to justify its actions and to make an accurate accounting of all of the funds it has received on Abingdon Pediatrics' behalf. Based on the evidence presented, I find that MEBS has failed to demonstrate the propriety of its agents' actions. I also

find that it has failed to properly account for all of the funds it received on Abingdon Pediatrics' behalf.

In particular, I find that Abingdon Pediatrics' accounts receivable totaled \$262,212.45 when MEBS took over Abingdon Pediatrics' patient billing and collections in January 1997. I further find that, in August 1998, Abingdon Pediatrics' accounts receivable totaled \$129,648.81. In reaching this finding, I specifically find the testimony of Mrs. Gardner regarding the operation and functioning of the Medic system and the meaning of the information contained in the Medic reports to be the more credible. I also find that the documentary evidence, including Plaintiff's Exhibit No. 2, supports her testimony. Therefore, I find that MEBS had a duty to account to Abingdon Pediatrics for the difference between these two amounts, which is \$132,563.64. I further find, however, that MEBS has accounted for only \$110,257.65. Included in this amount is the \$51,061.90 that was deposited into Abingdon Pediatrics' Nationsbank account, the \$38,763.01 collected on accounts more than 150 days old and deposited into ATS's Collection Accounts and the \$20,432.74 in Medicaid write-offs⁴. Thus, I find that MEBS has not accounted for \$22,305.99 of the funds that it or its agents received on behalf of Abingdon Pediatrics. That being the case, I will enter judgment in Abingdon Pediatrics' favor ordering MEBS to pay \$22,305.99 to Abingdon Pediatrics in addition to the \$6,552.64 still owed to Abingdon Pediatrics as part of its share of collections on accounts older than 150 days.

⁴While MEBS has not provided the court with any proof to support its claim that it properly deducted \$20,432.74 in Medicaid write-offs from Abingdon Pediatrics' accounts receivable, Abingdon Pediatrics has not contested this amount.

Based on the evidence presented to the court, I cannot determine what amount, if any, of this \$22,305.99 was deposited into the so-called Insurance Recovery Account and, ultimately, distributed to Stoots and Carter or their businesses. Despite the court's March 1999 order to file an accounting identifying each payment received by MEBS on behalf of Abingdon Pediatrics, the patient's account on which each payment was received and the bank account into which each payment was deposited, MEBS has never done so with regard to the sums deposited into the Insurance Recovery Account. The evidence before the court does show, however, that ATS filed a number of insurance claims, which, if paid by the insurer, were owed to the patients, not Abingdon Pediatrics. Furthermore, Stoots has admitted that none of Abingdon Pediatrics' patients ever gave MEBS or ATS permission to file claims on their behalf. Therefore, none of these patients ever agreed to pay any fee for the filing of these claims.

I also find that Abingdon Pediatrics did not request or authorize ATS to file any insurance claims, other than Medicaid and Medicare claims, and did not agree to pay ATS \$2.50 for each insurance claim filed. I reach this conclusion in large part based on my finding that Carter's and Stoots's testimony on this issue is not credible and is not supported by the documentary evidence. In particular, the documents produced by Stoots to support such an agreement show only that Dr. Gardner agreed to allow ATS to file Medicaid and Medicare claims on behalf of Abingdon Pediatrics. Also, Carter wrote letters which stated that MEBS, not Abingdon Pediatrics, contracted with ATS to file unfiled insurance claims and that the patients, not Abingdon Pediatrics, would be responsible for any fees associated with these filings. While Carter testified that Abingdon Pediatrics entered into a separate agreement with ATS to file these claims

and that MEBS had nothing to do with this agreement, he also admitted that he opened the bank account into which all payments on these claims were deposited. Also, the bank records show that this account was opened in the name of "MEBS/ATS; DBA: Insurance Recovery." Furthermore, Carter set up the account so that he, in addition to Stoots, was authorized to write checks on this account.

While both Stoots and Carter claim that the Gardners approved the establishment of this account and approved disbursement of funds from this account to cover ATS's fees, the documentary evidence shows otherwise. In particular, the September 17, 1997, letter from Mrs. Gardner to Stoots stated, "... I did not know that numerous bank accounts were to be used to deposit Abingdon Pediatrics' monies, please explain this to me." Also, Carter wrote letters implying that any amounts received from insurance filings were being held and not disbursed. Furthermore, Carter's and Stoots's own actions belie their claims that the Gardners knew of this account and had approved the disbursement of funds from it. Carter admitted that he did not provide any of the bank statements for this account to the Gardners. Both Stoots and Carter admitted that they did not report any disbursements from this account to the Gardners, despite specific, repeated inquiries by Mrs. Gardner.

Furthermore, if the court were to believe Stoots's and Carter's claim, the court would have to find that Abingdon Pediatrics agreed to pay ATS \$2.50 per claim to file more than 12,000 claims, none of which were likely to be paid by the insurer because they were filed too late and many of which, if paid, would not result in generating any

amounts owed to Abingdon Pediatrics. To put it frankly, such an agreement flies in the face of reason.

Abingdon Pediatrics also asserts that it is entitled to judgment holding that MEBS, by breaching its fiduciary duties, has forfeited any fees it earned under the Contract. I have reviewed the case law cited by the plaintiff in support of its position, and I note that each of these cases deals specifically with a real estate agent's forfeiture of his or her commission. *See Owen v. Shelton*, 221 Va. 1051, 277 S.E.2d 189 (1981). Since the plaintiff filed this cause in equity, however, this court has the power to craft an equitable remedy based on the parties' actions and culpability. *See Hecht Co. v. Bowles*, 321 U.S. 321, 329 (1944). That being the case, I find that the egregious facts and circumstances of this case warrant forfeiture of the amounts MEBS retained as its share of the collections accounts, \$13,567.05.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

As supplemented by the above summary and analysis, the undersigned now submits the following formal findings of fact and conclusions of law as required by Federal Rule of Civil Procedure 52(a):

1. Carter's and CMG's actions in entering into and performing services under the Contract were taken with either the actual or apparent authority of MEBS;

2. Stoots's and ATS's actions taken in handling Abingdon Pediatrics' patient accounts were taken with the actual authority of Carter and MEBS;
3. In performance of its obligations under the Contract, MEBS and its agents, Carter, Stoots, CMG and ATS, owed Abingdon Pediatrics the fiduciary duties of honest dealing and accounting;
4. MEBS, through the actions of its agents, Carter, Stoots, CMG and ATS, breached these fiduciary duties;
5. Abingdon Pediatrics' accounts receivable totaled \$262,212.45 when MEBS took over its patient billing and collections in January 1997;
6. Abingdon Pediatrics' accounts receivable totaled \$129,648.81 in August 1998;
7. MEBS has a duty to account for the \$132,563.64 difference between these two amounts;
8. MEBS has accounted for only \$110,257.65 of the \$132,563.64, leaving \$22,305.99 for which it has not accounted;
9. MEBS shall pay Abingdon Pediatrics this \$22,305.99;
10. MEBS also shall pay Abingdon Pediatrics the \$6,552.64 still owed of its share of collections on patient accounts more than 150 days old;
11. Abingdon Pediatrics did not request or authorize ATS to file any insurance claims other than claims with Medicaid and Medicare;
12. MEBS, through the actions of its agents, has forfeited any right to the \$13,567.05 it retained as its share of payments on patient accounts more than 150 days old; and

13. Judgment will be awarded in Abingdon Pediatrics favor against MEBS in the amount of \$42,428.68.

CONCLUSION

Based on the above-stated reasons, I find that MEBS, through its agents, violated the fiduciary duties it owed to Abingdon Pediatrics and has failed to pay over all sums owed to Abingdon Pediatrics. Therefore, final judgment will be entered in favor of Abingdon Pediatrics and against MEBS in the amount of \$42,428.68.

DATED: March _____, 2002.

UNITED STATES MAGISTRATE JUDGE