

PHYSICIAN COMPENSATION ARRANGEMENTS: CEO PITFALLS

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One of the major challenges facing Hospital CEO's today is the negotiating of financially prudent and legally compliant Physician Compensation Arrangements. Indeed, with increasing pressures from physicians and Hospital Boards, CEO's are often placed in the unenviable position of constructing these agreements within the constraints of commercial reasonability and fair market value regulatory requirements, while balancing the financial (and emotional) issues associated with these transactions. The major pitfalls and considerations to assist Hospital CEO's in this delicate area of responsibility are as follows:

I. MONITORING PHYSICIAN CONTRACTS

- **It is not uncommon for hospitals to have contractual agreements with independent physicians for services such as employment agreements, medical directorships, office space leases, on-call arrangements, emergency department coverage agreements, recruitment agreements and other professional services agreements**
- **Many hospitals focus on the initial physician contract development itself, taking steps so that appropriate provisions are included and that the contract is fully analyzed by the legal department of the hospital or by outside counsel**
- **It is important to monitor these arrangements to ensure that they continue to remain in compliance (i.e., renewal terms, expired contracts, etc...)**

II. IMPORTANT LAWS TO CONSIDER IN DEVELOPING AND MONITORING PHYSICIAN CONTRACTS

(a) ANTI-KICKBACK STATUTE

- **Federal anti-kickback law generally prohibits the provision of any economic benefit in exchange for the referral of patients or business that will be reimbursed under any federal health care program**
- **Physician Contracts should meet an applicable safe harbor under the Anti-kickback statute**

(b) THE STARK LAW

- Stark Law prohibits a physician from making referrals for “designated health services” to entities with which the physician or immediate family member has a direct or indirect financial relationship
- Only applies to Medicare DHS services (i.e. inpatient and outpatient hospitalization services, clinical laboratory services, radiology services, etc.)
- Strict Liability Law – Whether you intend to violate this law does not matter!
- Physician Contracts should meet an applicable exception to the Stark Law

III. SAFE HARBORS AND EXCEPTIONS MOST APPLICABLE TO PHYSICIAN CONTRACTS

- Rental of office space or equipment
- *Bona fide* employment relationships
- Personal service agreements
- Physician recruitment

(a) PERSONAL SERVICE ARRANGEMENTS

- The agreement is in writing, signed and specifies the services covered
- The arrangement includes all services provided by the physician (can be multiple agreements if they all reference one another)
- Services must be reasonable and necessary
- The term of the agreement is at least 1 year
- The compensation is set in advance, does not exceed FMV and does not take into account volume or value of referrals
- Services do not involve recommending or promoting of a business arrangement

(b) LEASES

- The agreement is in writing, signed and specifies the space or equipment to be leased
- The term of the agreement is at least 1 year

- The space or equipment leased is reasonable and necessary
- The rent is set in advance and consistent with FMV
- Rent payment does not take into account volume or value of referrals
- The lease would be commercially reasonable in absence of referrals

IV. PROBLEM AREAS WITH PHYSICIAN CONTRACTS

The most common issues hospitals may discover in reviewing their physician contractual arrangements can include:

- Expired contracts
- Financial relationships where no written contract ever existed
- Undocumented modification of financial terms (i.e. parties failed to amend the contract)
- Terms modified during the first year in violation of safe harbors and exceptions available under the Anti-Kickback Statutes and Stark Law
- Agreements that incorrectly describe the services being provided
- Hospital benefits to a doctor that exceed Stark's minimum exception, (i.e. non-monetary compensation such as advertising, meals, parking, etc...)
- Allowing physicians to begin work without being substantially credentialed, opening the possibility of physicians working without expectation of professional reimbursement principally to enhance and/or capture technical revenue

V. OTHER POTENTIAL PROBLEM AREAS INCLUDE:

- Non-enforcement by hospital of late payments or non-payment for certain months or a lengthy period of time
- Lack of current and/or appropriate fair market value documentation to support contractual arrangement
- Payments that do not match terms of the agreement
- Fair Market Value vs. Commercially Reasonable
- Changed or reduced responsibilities without applicable amendments to the effective contract

- **Missing or inadequate timesheets or other documentation to support hourly payments**

VI. OBSERVATIONS AND LESSONS FROM SOME RECENT COURT CASES REGARDING PHYSICIAN CONTRACTUAL ARRANGEMENTS

- **A long-term arrangement should be reviewed periodically for compliance**
- **An arrangement should include enumerated administrative duties if part of the compensation is in return for performing those duties**
- **In general, compensation should not exceed the 75th MGMA percentile unless there is a very legitimate reason, i.e, physician practice being in a Health Professional Shortage Area (HPSA) or Medically Underserved Area (MUA)**
- **Physician benefits should be consistent with those provided to other hospital employees**
- **Fair market value and commercial reasonableness should be established prior to the effectiveness of the arrangement**
- **Paying physicians for loyalty is not permissible**
- **Generally, arrangements where it is mathematically impossible for the provider to make money or break even, are suspect**

VII. FAIR MARKET VALUE (FMV) AND COMMERCIAL REASONABILITY ARE VERY IMPORTANT FACTORS TO CONSIDER WHEN CONTRACTING WITH YOUR PHYSICIANS

- **The IRS prohibits 501 (c)(3) tax exempt entities from operating other than for charitable purposes. Hence, the IRS prohibits payments in excess of fair market value**
- **Stark law defines fair market value as the "value in arm's length transactions, consistent with the general market value"**
- **To be commercially reasonable, both the services and the payment must be commercially reasonable**
- **Reasonable compensation is the amount that would ordinarily be paid for like services by like enterprises under like circumstances (I RC Section 162)**

(a) ESTABLISHING FMV: THE SURVEY APPROACH

Survey firms to use for survey data include, but are not limited to:

- The Medical Group Management Association - www.MGMA.com
- Sullivan Cotter and Associates, Inc. - www.SullivanCotter.com
- Hospital & Healthcare Compensation Services - www.HHCSINC.com
- Integrated Healthcare Strategies (f/k/a Clark Consulting) - www.IHStrategies.com
- Towers Watson (f/k/a ECS Watson Wyatt Data Services) - www.TowersWatson.com
- The Hay Group - www.HayGroup.com
- William M. Mercer - www.Mercer.com
- American Medical Group Association - www.AMGA.co

VIII. PHYSICIAN CONTRACT MODELS/OPTIONS

1. Hospital Employment
2. Independent Private Practice
3. Independent Rural Health Clinic
4. Physician Enterprise Model
 - a. Practice Leasing
 - b. Collections Guarantee Fee
 - i. Similar to hospital based physician arrangements
5. Incentive Compensation Payments based upon Qualitative Benchmarks

IX. CONSIDER MAINTAINING A PHYSICIAN CONTRACTS DATABASE TO MONITOR YOUR PHYSICIAN CONTRACTS

Hospitals should consider creating and maintaining a database of existing, new or renewed physician contractual arrangements potentially including the following:

- The identity of the parties and term of the contract
- Description of goods and services provided under the arrangement
- Compensation methodology

- **Amount and documented fair market value for each transaction, preferably by an independent third party**
- **This will help you ensure that your Physician contracts remain compliant**

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