ELIMINATING THE MYSTERY OF FAIR MARKET VALUE

Practical Insights for Provider Organizations

Learning Objectives

- Describe the regulatory environment requiring FMV compliance
- Explore common valuation approaches for physician compensation
- Identify commercial reasonableness in common physician arrangements
- Discover techniques to elevate your organization's FMV compliance
The Contracting and Compliance Environment

- Shift in Compliance Enforcement Focus
  - Compliance is not just a reimbursement and privacy issue
  - The largest hospital settlements and government’s fraud and abuse focus is on hospital / physician financial relationships

- Key Legal Considerations
  - Stark Law
  - Anti-Kickback Statute
  - IRS Rules for Tax-exempt Organizations
  - Civil Monetary Penalties

Daniel Levinson, HHS OIG
Recent Enforcement Actions

- **Erlanger (2005) – The Poster Child**
  - $40 Million Stark and Anti-kickback settlement in October of 2005
  - The investigation focused on:
    - Physicians’ relationship with hospital
    - Contracts involving physicians who served on the Erlanger Board
    - Board members and possible conflicts of interest
    - Records of hospital’s compliance program
    - Time records / supporting documentation for medical directors
  - Erlanger general counsel said activities at Erlanger “were perfectly consistent with what a lot of hospitals have done. It is unfortunate that Erlanger has to be the poster child.” The Chattanoogan.com
  - As part of this settlement, federal officials said they planned to vigorously prosecute others as well.

Enforcement...

- **Tuomey**
  - Qui tam lawsuit brought by whistleblower
    - Alleged that part-time physician employment agreements entered into by Tuomey were above fair market value and not commercially reasonable
    - Notable that Tuomey had obtained fair market value opinions approving the arrangements
  - Jury held that Tuomey violated the Stark Law, but not the False Claims Act
  - Court subsequently awarded $44.9 million (plus interest) in damages to the government related to Stark Law violations
  - Court also ordered a new trial on the issue of False Claims Act liability
    - Up to $275 million in additional damages and fines at stake
  - Case being re-litigated
WASHINGTON – The United States has partially intervened in a lawsuit under the False Claims Act against Halifax Hospital Medical Center and Halifax Staffing Inc. in the U.S. District Court for the Middle District of Florida, the Department of Justice announced today.

The government partially intervened with respect to allegations that Halifax, which is located in Daytona Beach, Fla., violated the Stark law, which prohibits a hospital from billing Medicare for services referred by physicians that have an improper financial relationship with the hospital. The United States alleges that Halifax’s contracts with three neurosurgeons and six medical oncologists were improper, in part, because they either paid physicians more than fair market value, were not commercially reasonable or took into consideration the volume or value of the physicians’ referrals.

“Improper financial arrangements between hospitals and physicians threaten patient safety because personal financial considerations, instead of what’s best for the patient, can influence the type of health care that is provided,” said Tony West, Assistant Attorney General for the Civil Division of the Department of Justice. “The department is committed to preventing kickbacks that can corrupt the integrity of health care delivery.”

“The Stark law was enacted to prevent financial ties between a physician and an entity providing health care services from influencing the level of care provided to a patient,” said Robert E. O’Neill, U.S. Attorney for the Middle District of Florida. “By bringing cases such as this one, we hope to ensure that precious health care resources are not being wasted as a result of questionable financial relationships between health care providers.”

The lawsuit was initially filed in July 2009 by Elin Baklid-Kunz, currently employed at Halifax Staffing as the director of physician services, under the whistleblower provisions of the False Claims Act. Those provisions authorize private parties to sue on behalf of the United States, and permit the United States to intervene and take over the lawsuit. The whistleblower is entitled to receive a portion of any recovery. In this case, the United States elected to intervene in only a portion of the allegations asserted by Ms. Baklid-Kunz.

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Legal / Regulatory Complexity

- Many Landmines
  - Exceptions and Safe Harbors
  - Strict Guidelines
- Government Direction Not Always Clear
  - What constitutes a referral? Is it DHS?
  - Gray Areas
- Financial Terms Critical
  - Fair Market Value
  - Commercial Reasonableness
### Common Physician Arrangements

- Employment Agreements
- Professional Service Agreements
- Medical or Program Directorship Agreements
- Service Line Co-Management Agreements
- Call or Clinical Coverage Agreements
- Independent Contractor Agreements
- Shared Use or Cost Agreements
- Lease Agreements
- Management Service Agreements

### Common Relationships

<table>
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<tr>
<th>Traditional</th>
<th>Unique</th>
<th>Emerging</th>
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| • Employment  
  • Medical Directorship  
  • Call Coverage  
  • Independent Contractor  
  • Recruitment  
  • Medical Staff Leadership  
  • Mid-Level Supervision  
  • Leases | • Professional Services Arrangements (PSA)  
  • Co-Management Arrangements  
  • Income / Revenue Guarantees  
  • Uncompensated Care  
  • Management Services Arrangements (MSA)  
  • State/county subsidies to physicians through hospitals, etc.  
  • GME / Teaching Programs and Resident Supervision | • Research Relationships  
  • Technology: Meaningful Use / CPOE / EHR Champions  
  • Specialty Clinics (e.g., wound care, vein, outreach, etc.)  
  • Shared savings and bundled payments  
  • Risk-Sharing Arrangements  
  • ACOs |
Fair Market Value

Stark Law imposes limits on the valuation of certain income under compensation arrangements.

- “Usually, the fair market price is the price at which bona fide sales have been consummated for assets of like type, quality, and quantity in a particular market at the time of acquisition, or the compensation that has been included in bona fide service agreements with comparable terms at the time of the agreement, where the price or compensation has not been determined in any manner that takes into account the volume or value of anticipated or actual referrals.”
- Stark further states that FMV may be determined by “any reasonable method.”
- Former Stark Safe Harbor sought to define FMV for hourly compensation arrangements. Ultimately deemed impractical.
Valuation Approaches

- **Income Approach**
  - Value determined by reference to expected future income generated

- **Cost Approach**
  - Value determined for an asset based on economic principle of substitution

- **Market Approach**
  - Value derived from analysis of comparable data / transactions

Valuation of Physician Compensation Arrangements

- Determination of appropriate payment terms for physician services (professional, administrative, other)

  - **Market approach is most prevalent**

  - Mixed and emerging perspectives among appraisers

Valuation Art and Science

- The determination of FMV in the context of physician compensation is a mix of art and science.
  - “Science”
    - Incorporates methods and observes principles applied in traditional business valuation
    - Some methods not applicable to physician compensation
  - “Art”
    - Legal / regulatory direction is not always clear
    - Data is not perfect or may not even be available
    - Apply or devise different valuation models and assumptions to best reflect arrangement being valued

- And, the payment arrangement still must be commercially reasonable.
Assumptions: Value Drivers in Representative Arrangements

**Employment**
- Prevailing specialty compensation
- Amount and type of physician work
- Physician qualifications / experience
- Market factors
  - Recruitment / retention
  - Supply and Demand
  - Competition
  - Payer Climate

**Professional Service Arrangement**
- Prevailing specialty compensation
- Amount and type of physician work
- Physician qualifications
- Market factors
- Expense considerations

**Emergency Call**
- Prevailing specialty compensation
- Call Requirement (unrestricted or restricted)
- Number of participating physicians and burden of call
- Intensity of Call
- Payor Mix
- Hospital trauma designation
- Market factors

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**Balancing Risk**

- **Employment Compensation Assumptions**
  - New vs. Established Physician
  - Abundant Supply vs. Critical Community Need
  - Guaranteed Salary vs. At-risk Compensation
  - Additional Duties vs. Protected Time
  - Low Producer vs. High Producer

- **Market Data Context**
  - Lower Risk – 25th ptile to Median
  - Moderate Risk – Around the Median
  - High Risk – Median to 75th ptile
  - Highest Risk – Greater than 75th ptile
FMV: The Secret Recipe

- Paying a Physician More than 75th Percentile may be OK, but...
  - KNOW the MARKET
  - CLARIFY (quantify) the ASSUMPTIONS
  - ASSESS the RISK

- AND...the terms must be commercially reasonable

FMV

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FMV...a simple illustration

- New Family Physician (w/o OB)
  - 1-year guaranteed salary, no extraordinary duties, abundant supply and desirable community

- Family Practice Compensation Data

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- Multiple survey sources, 2011.

- What's Fair Market Value?
FMV…a more complex illustration

- Highly Successful Neurosurgeon
  - Hospital has been unable to retain surgeons and is at-risk of losing trauma designation
  - Will serve as program medical director and conduct research
  - Required to provide 15 days of call per month
  - Physician wants a guarantee plus incentives and is aware of several recent placements offering compensation over $1 million

- Compensation Data

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* Market Examples.

- What's Fair Market Value?

SECTION III

Commercial Reasonableness in Physician Arrangements
Critical Requirements of Setting Physician Contract Payment Terms

- Stark Exception
- AKS Safe Harbor
- IRS – Rebuttable Presumption

Legal

Fair Market Value
- Appropriate Method and Assumptions

Commercially Reasonable
- Makes good business sense
- Is explainable

Commercial Reasonableness

- Required, but not defined in Stark or AKS

- CMS Definition
  - An arrangement that appears to be a sensible, prudent business agreement, from the perspective of the parties involved, even in the absence of any potential referrals.

  - “An arrangement will be considered ‘commercially reasonable’ in the absence of referrals if the arrangement would make commercial sense if entered into by a reasonable entity of similar type and size and a reasonable physician (or family member or group practice) of similar scope and specialty, even if there were no potential DHS [Designated Health Services] referrals.”

- Heightened concern as a result of Toumey and Halifax cases.
Commercial Reasonableness:
A Practical Concern

“A payment term may be deemed to be fair market value, but may not be commercially reasonable."

Key Questions
- Is the arrangement prudent, and why?
- Does it make good business and economic sense?
- Are the payment terms “reasonable”?
- Is the arrangement consistent with others in the industry?
- Do payment terms exclude the value and volume of referrals?

Commercial Reasonableness:
Case #1

Before entering into a lease agreement with a physician group for MOB space, you obtain a FMV opinion of lease rates for similar real estate.

- The terms of the lease are based on the FMV lease rate applied to 3,000 square feet of MOB space that the parties estimate is needed.
- Two years after the lease agreement is executed, the hospital is only using 1,500 square feet but the contract is not amended.

- Is the lease arrangement commercially reasonable?
Commercial Reasonableness:
Case #2

☐ You employ a group of hospitalists who are paid a base salary and can earn incentive compensation based on WRVUs.
  ☐ You are having trouble getting night shifts and weekend shifts covered, so you offer extra shift payments to the employed hospitalists.
  ☐ During the extra shifts, they generate WRVUs.

☐ Is it commercially reasonable to provide WRVU credit for coverage of extra shifts?
  ☐ Why or why not?

Commercial Reasonableness:
Case #3

☐ There are three competing hospitals in your local area. Historically, none of these hospitals have paid for ED call.
  ☐ The non-employed orthopedic surgeons on your medical staff request $1,000 per night for call.

☐ If no other hospital is paying for call, is it commercially reasonable for your hospital to pay for call?
  ☐ What factors might make it commercially reasonable?
A private practice physician you have identified as the future of a key program has been offered a position in another market.

- You propose a counter offer (employment) that includes salary for full-time clinical services and additional pay for medical director services.
- Due to an adequate supply of other physicians in the same specialty, productivity is predicted to be low in the near term.
- Another physician is already performing medical director services in the same clinical area.

Is it commercially reasonable to combine pay ("Stacking") for the arrangements? Why or why not? What additional information do you need?

- If the physician joined a group that has a PSA with your hospital, would it be commercially reasonable to consider benefits and practice operating costs in the offer?

Commercial Reasonableness

- Considerations
  - Stacking of arrangement(s)
  - Opportunity to generate fees / profit
  - Term / termination of arrangement
  - Expected Losses
  - Ability to obtain item / services from other, less costly sources
  - Others
Elevate Your Organization’s FMV Compliance

Top Misconceptions in Physician Compensation Compliance

“So long as we do not exceed payment amounts above 90th percentile of MGMA, we are OK.”

“The contract says the doctor is here for 10 hours per week, therefore, we pay him for 10 hours.”

“The doctor is a ‘high producer’, which is why base salary is set at the 75th percentile.”

“The other hospital in town pays $2,500/night, so that must be fair market value.”

“We can pay the doctors for call; because if we don’t, they’ll go to the competing hospital.”

“The physician is employed, thus, the Stark Law doesn’t apply.”
Other Misconceptions in Physician Compensation Compliance

- **Misapplication of Units**
  - “The neighboring hospital pays $1,000 per visit for ROP screenings.” *Contract actually states $1,000 per month.*
  - “Our trauma program is covered by a traumatologist during the day, and we pay community surgeons for trauma call on a 24-hour basis.”
  - “In the service agreement, cost data for non-physician provider benefits per FTE physician applied to non-physician provider FTEs.”

- FMV opinion included critical governing assumptions that were not applied in the executed contract.

- Practice acquisition/asset purchase FMV and go-forward physician compensation are unrelated.

WRVU Models Gone Wrong

- **Common errors in measuring WRVUs**
  - “Total” vs. “work” RVUs
  - GPCI adjustments
  - Assistant surgery (80, 81, 82 modifiers)
  - Co-surgery (62)
  - Bilateral (50) and multiple procedures (51)
  - Mid-level providers
  - Site-of-service differentials
  - CMS changes in WRVUs
  - New or discontinued CPT codes

- **Common errors in applying compensation to WRVU data**
  - 90th percentile producer so 90th percentile $/WRVU applied
What do you know about physician contracting in your organization?

1. Are physicians employed or independent contractors?
2. Is there a contract approval process and who is involved (board, legal, finance, compliance)?
3. Do physicians have written agreements?
4. How are physicians compensated (production, fixed rate, hourly)?
5. Is FMV determined and documented? How?
7. Is the compensation structure periodically reviewed?
8. Does physician compensation include ancillaries or only personally performed services?
9. Do physicians complete and submit time records for non-clinical time?
10. Do contracts meet a Stark exception? Anti-kickback safe harbor?
11. Is the POS billed correctly for physician services?

Elements of a Compliant Physician Relationship

- Stark exception or AKS safe harbor is identified and followed
- Agreement in writing
- At least one-year term
- Compensation set in advance
- Compensation not tied to referrals (past, present or future)
- Compensation is fair market value and commercially reasonable
Elements of an effective physician compensation compliance program

- Consistency is key
  - Apply compliance policies consistently.
  - Apply data consistently. Avoid cherry-picking.

- Understand the data
  - Be aware of survey bias.

- Know when an outside opinion is needed
  - Certain arrangement types, physician relationships, or dollar amounts may need a third party review.

- Ensure appraiser’s assumptions match the agreement.

Why is valuation knowledge relevant to the Compliance Officer?

- Evaluate
  - Perform review and analysis of compensation arrangements
  - Support audit efforts
  - Identify outlier contracts that may need focused review

- Critique
  - Review work of outside appraisers
  - Reliability and defensibility

- Explain
  - What valuation methods were used
  - What influencing factors were relevant

- Consistency and Compliance
  - Establish policy and promote go-forward compliance

- Efficiency
  - Build internal capacity and save money
Questions?

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APPENDIX I

Commercial Reasonableness Assessment
Evaluating and Documenting Commercial Reasonableness – 1

1. What is the hospital's specific purpose for contracting for the services or conducting the transaction?

2. Does the arrangement meet the need/demand for the services of the hospital and surrounding community? Is there any objective data available that indicates a hospital and community need for these specific services?

3. Absent patient referrals, what benefits do the hospital and community receive from the arrangement?

4. Does entering into the arrangement solve or prevent an identified business problem for the hospital?

5. Are the terms of the arrangement sensible and consistent with accepted business practices?
   - Factors to consider include: duration, renewal, termination, compensation review and other relevant contractual terms.

Evaluating and Documenting Commercial Reasonableness – 2

6. Is the arrangement explainable? In other words, on its face, is the arrangement clear and are the tasks, duties, and responsibility expectations clearly articulated and documented?

7. Absent patient referrals, does the agreement make economic sense for both parties?

8. Is the arrangement consistent with other arrangements of similar nature observed in the industry?
Evaluating and Documenting Commercial Reasonableness – 3

EXAMPLE: Medical Directorships

1. Is the scope of the directorship duties reasonable and consistent with other comparable directorships in the industry?

2. Is there thorough documentation of administrative and clinical responsibilities (percentage of time and amount of time expended for each)?

3. Are there internal review processes to assure/verify the director is performing the expected duties, tasks, and responsibilities?

4. Have you assured, prior to entering into the arrangement, that there will be no duplication of services or medical staff requirements as a result of the arrangement?

5. Are there multiple directorships and if so, are there policies/procedures to assure that there is no duplication of actual services provided?

6. Are the terms of the directorship agreement reasonable and consistent with business practices?
   - Factors to consider include: duration, renewal, termination, compensation review and other relevant contractual terms.

Assessing Value Drivers: Physician Work Effort

- Types of service
  - Clinical
  - On-call / Availability
  - Administrative

- Sources of support for amount of work
  - Clinic coverage schedules
  - Productivity measures (WRVUs)
  - Call schedules
  - Time sheets / attestations
  - Physician/management perspectives
Assessing Value Drivers:
Physician Qualifications / Experience

- Years of experience are less predictive of compensation than other variables
- Key Opinion Leader / Thought Leader
  - National recognition
  - Academic appointments
  - Research / publications
  - Innovations
- Exclusive provider of specialized procedure(s)

Assessing Value Drivers:
Expense Considerations

- Practical standards for expense considerations in independent contractor arrangements
  - Limited definition / guidance from government
  - Perspectives among appraisers may differ
  - Organization’s philosophy is important
- Avoid paying for excessive benefits
- Understand cost survey data
  - e.g., Non-physician provider benefits per FTE physician
Assessing Value Drivers: Specialty Compensation

- Published survey data is the most common / “reliable” source of prevailing specialty compensation
  - Market approach often relies on multiple data sources
  - Important to understand what the data represents
    - Relationship between compensation and compensation per WRVU

- Market comparable data may be useful as well
  - Emerging/small specialties for which survey data does not exist
  - Local color

- Must be “arm’s-length”