STROUDWATER

Fair Market Value and Right Sizing Physician Compensation

***"It was like that when I got here."* - Homer Simpson**

By Mike Fleischman, Stroudwater Associates

We've heard this phrase exclaimed several times recently by newly appointed CEOs and CFOs who have inherited dysfunctional, and in some cases legally questionable, employment and medical director agreements with their staff physicians. The Inspector General's office of HHS is now focusing greater attention on compensation plans for physicians employed by hospitals and health systems. Outcomes of this increased scrutiny include:

- A Midwest hospital's agreement to pay the United States $34M to settle alleged False Claims Act violations arising from improper payments to oncologists
- A Florida health system's settlement to the federal government of $69.5 million for alleged violation of the False Claims Act by engaging in improper financial relationships with nine physicians
- A Florida nonprofit's $118.7 million agreement to settle claims that it paid bonuses to employed physicians based on a formula that improperly took into account the value of the physicians' referrals

Our industry now faces the promise of increased scrutiny of physician compensation plans combined with the need to recruit and retain physicians from a shrinking supply pool in an increasingly competitive landscape. This pressure has resulted in hospitals and health systems stretching the rules. If you're one of the newly appointed CEOs or CFOs who have inherited some poorly structured physician employment deals, consider that they need to be restructured to comply in ways that are at fair market value and reasonable. In other words, they must be able to withstand the scrutiny of the HHS-OIG and the IRS.

Two statements from the September 2015 settlement of *United States ex rel. Reilly v. North Broward Hospital District, et al sum up the importance of exercising due diligence in developing and maintaining physician compensation plans.*

- "Our citizens deserve medical treatment uncorrupted by excessive salaries paid to physicians as a reward for the referral of business rather than the provision of the highest quality healthcare," said U.S. Attorney Wifredo A. Ferrer of the Southern District of Florida. "This office will be steadfast in continuing to devote all necessary resources to ensure that anyone rendering medical care does so for the sole benefit of the patient and in compliance with the law."
- "Improper financial rewards given to physicians in exchange for patient referrals corrupts medical decision making and inflates health care costs," said Special Agent in Charge Shimon R. Richmond of the U.S. Department of Health and Human

> Services-Office of Inspector General (HHS-OIG). "Our agency will continue to root out such behavior from our health care system."

As with any aspect of compliance, the development and dedicated utilization of standard policies and procedures is key. We recommend, for example, setting limits on annual CME allowance, time off, dues and subscriptions, and life, health, and disability insurance for all physicians employed by the institution. While the group of physicians can certainly have a benefits structure that differs from that of other employees, we do not recommend "side deals" or additional levels of benefits for certain individuals.

The first step toward bringing dysfunctional (or worse) employment agreements into compliance is to review the historic compensation paid to the physician and compare it to his or her production. The review should also acknowledge any administrative responsibilities that the physicians have in addition to their clinical role, such as directorships, teaching, and supervision of advanced practice practitioners. Also, consider how value or quality measures play into the equation. Some hospitals only measure quality in terms of patient satisfaction, while others are becoming more sophisticated and are measuring clinical outcomes. Still others are not yet measuring anything related to quality.

While creating reasonable and compliant employment agreements is half the battle, we are still left with the issue of recruiting physicians in the current, highly competitive industry environment. Given our extensive work in rural areas, our team at Stroudwater is quite familiar with the challenges that exist recruiting physicians and other healthcare providers. As with any planning and implementation activity, there must be a process in place. The transition to value-based reimbursements and bundled payments will make the process more complex, and while there is some room for creativity, don't overshoot the mark. A thorough understanding of what is happening in the marketplace should guide the process, and keep in mind the following lessons we've learned along the way.

- **It only takes one.** Under the False Claims Act, only one person has to file a complaint. Healthcare organizations can no longer be willing to brush aside the potential risks. Whistleblower provisions aid the government in helping to ensure compliance. While all whistleblower claims are not valid, all such claims must be reviewed. There is a clear financial incentive to "blow the whistle" that compensates the whistleblower based on the size of the claim. In the infamous Tuomey case of more than $237 million, the whistleblower could receive in excess of $11 million for filing a complaint under the False Claims Act.
- **Small errors add up quickly,** and with compensation issues, penalties grow quickly, too. Some of these risks cannot be covered by an insurance policy.
- **Know your market.** Compensation must reflect "fair market value" and be "commercially reasonable." Paying compensation in excess of collections poses significant risk. Appropriately structured employment and compensation arrangements may help mitigate this risk, depending on how the arrangements are designed. Know

that it is imprudent to overly rely on survey data – national or even regional median does not automatically constitute fair market value, particularly if other factors specific to the hospital's market and the specific physician are not considered.

- **Be creative—but not that creative.** Given the narrowing market base, the increased workload expectations, and the changes being wrought by healthcare reform, organizations are already struggling to recruit physicians. So, it is no surprise that healthcare providers are seeking new ways to attract and retain talent—and pulling compensation as a major lever.
- **It's a process.** For those healthcare providers seeking to launch innovative compensation models, it may not be enough to just consider redesign. The full range of transformation issues plaguing the market must also be taken into account.
- **It's complicated.** Physician arrangements can be complex and require seasoned advisors to help mitigate any risk. Note the comment made by Judge Wynn in a separate Concurring Opinion on the Tuomey case, suggesting this is an area of complexity under both the Stark Act and the False Claims Act, compounded by the laws and rules regulating Medicare: "I am troubled by the picture this case paints: An impenetrably complex set of laws and regulations that will result in a likely death sentence for a community hospital in an already medically underserved area."

Finally, make sure that your board understands that final decisions on compensation arrangement are their fiduciary responsibility. They must be informed as to the need for the arrangement and be assured that it meets the test of reasonableness and fair market value.

"It was like that when I got here" may have worked occasionally for Bart or Homer Simpson, but the chances of any federal court accepting it as a point of defense are likely non-existent. Leaders must be ready and accountable, and Stroudwater can help.

Mike Fleischman *brings more than 40 years of experience in the healthcare industry to each client engagement. As a consultant, his focus is on helping providers develop integrated clinical systems, including physician-hospital relations, medical group strategic planning, group governance, medical staff development plans and community needs analysis, practice operational assessments, PCMH development, and HIPAA.*