The Ins and Outs of Physician Practice Lease Arrangements to Achieve Hospital and Physician Objectives

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Objectives

Review examples of practice lease arrangements for professional services and practice resources.
Discuss objectives that may lead hospitals and physicians to pursue a lease arrangement.
Illustrate the variation of specified services and the assignment of business risk
Address the impact of these variations in relation to the valuation.
Review potential regulatory hazards and compliance considerations.
Provide practical tools to avoid common misunderstandings and develop best practices for implementation and integration.
Present specific cases and “war stories” from prior experience.

Overview of Physician Practice Lease Arrangements

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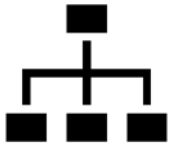
Continuum of Physician-Hospital Transactions

EMPLOYMENT | **ALTERNATIVE ARRANGEMENTS** | **INDEPENDENCE**



Tighter — Degree of Alignment — *Looser*

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ALTERNATIVE ARRANGEMENTS

Physician services contracts

- Call-coverage
- Medical director
- Co-management
- Other arrangements

Joint Ventures

- MSO JV
- Ambulatory Surgery Center (ASC) JV
- Equipment Ownership
- Site expansion

"Leases" and other contractual arrangements

- **Professional services agreement**
- **Practice resources agreement**
- Practice support models
- Captive affiliate model

Clinical Integration

- Accountable Care Organizations (ACOs)
- Independent Practice Associations (IPAs)
- "Narrow" clinically integrated network arrangements

Practice "Lease" Defined

- ***Lease:*** A contract by which one conveys real estate, equipment, or facilities for a specified term and for a specified rent.
- ***Operating Lease:*** A contract that allows for the use of an asset but does not convey ownership rights of the asset
- ***Practice Lease:*** For our discussion the resources conveyed may include:
  - Professional services (provided by physicians and/or advanced practice clinicians) through a Professional Services Arrangement (PSA); or
  - Practice Resources (all of those other resources required to deliver the professional services including Space, support staff, equipment, supplies, etc.) through a Management Services Arrangement (MSA)

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Where are we going? And Why?

- ***What's the end-game?***
  - Exclusivity?
  - Full acquisition?
  - Phased transactions?
  - Move beyond "stabilize"
- ***What are the goals in the meantime?***
- ***Risk and Reward?***
  - What are the trade offs?

Unique transactions are not a "quick and dirty solution"

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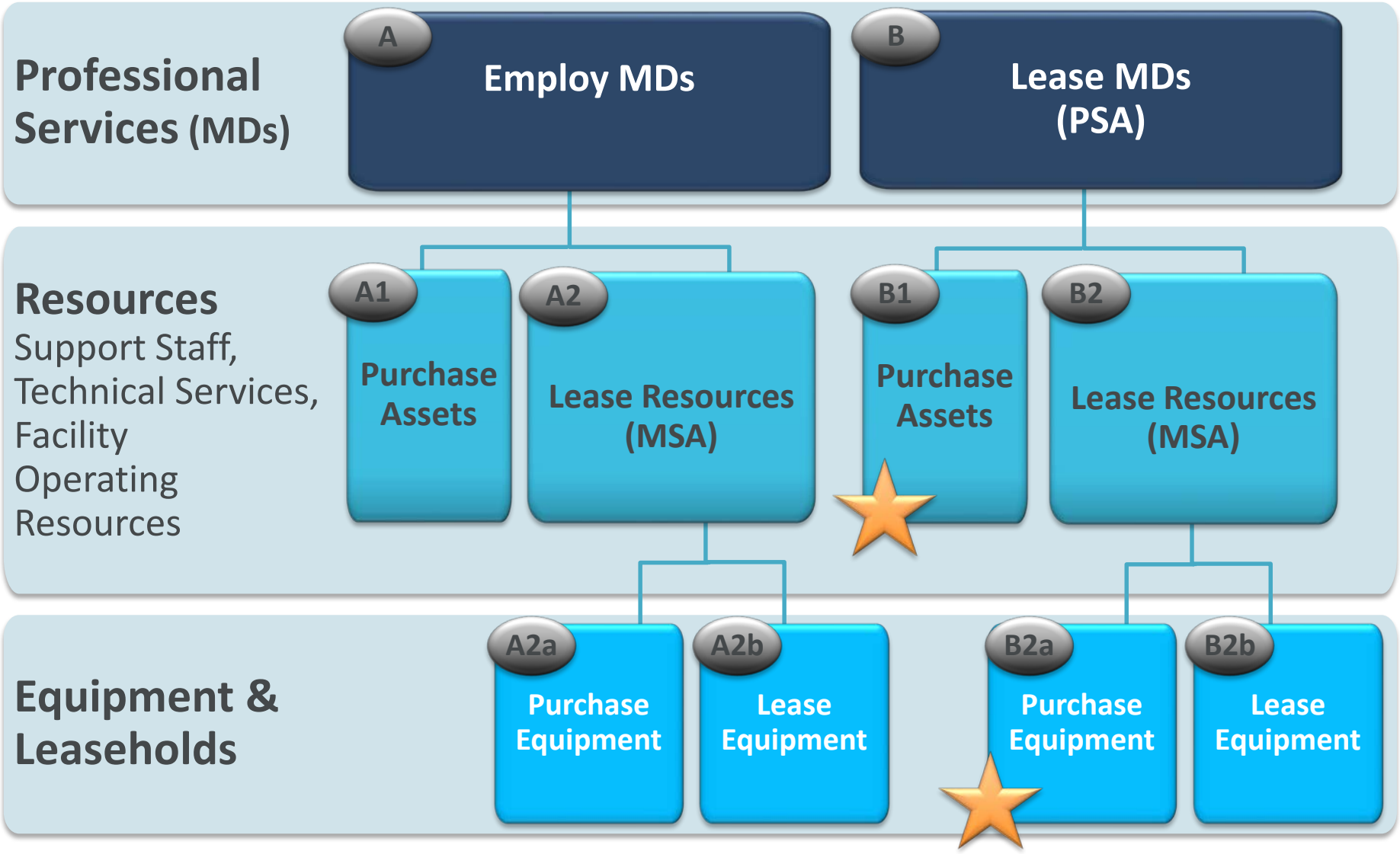
Choose Your Own Adventure…



Advantages and Disadvantages

Hospital's Perspective

Advantages

- Hospital bills and collects for all professional services provided by group practice physicians using its own rates (typically better if provider-based)
- Can "test the waters" with the group
- Groups may be less hesitant to be leased than employed
- Ability to expand clinical service offerings
- Preempt competition

Disadvantages

- Group is not fully integrated with the Hospital
- Hospital gives up some degree of control
- Payor mix risk shifts to Hospital
- Collections risk shifts to Hospital
- Lower level of physician commitment than employment model
- More regulatory risk than straight employment

Group's Perspective

Advantages

- Group makes compensation decisions – retain current benefits
- Physicians don't need to be running day-to-day operations
- Group practice stays in tact – patients don't see a change
- Physicians still practicing at the same site
- Physicians receive guaranteed revenue and a one-time payment in exchange for the assets sold
- Can sever ties easier with hospital if needed

Disadvantages

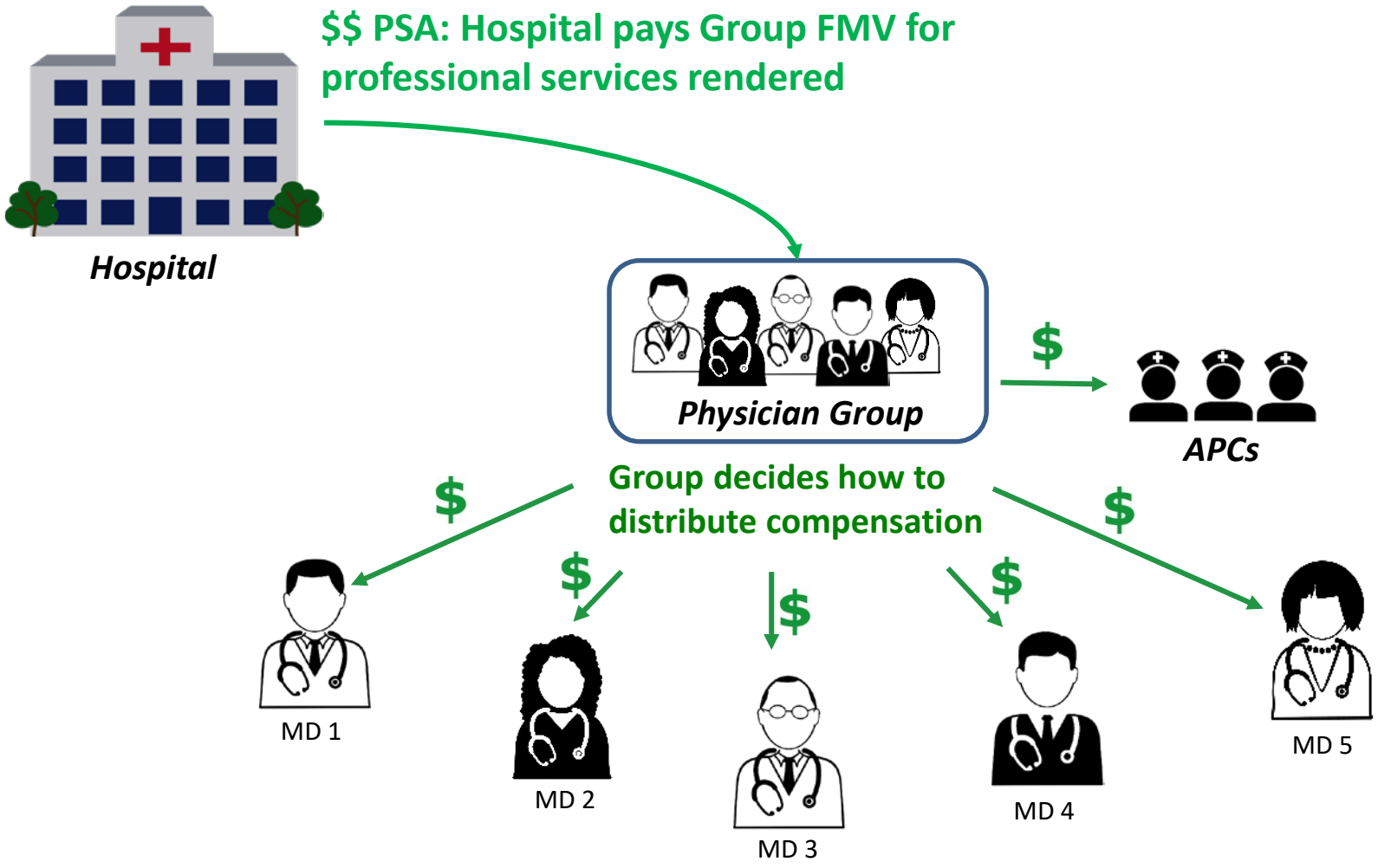
- Group is not fully integrated with Hospital
- Unwind can be difficult
- Some loss of control (depending on degree Hospital requires compliance with Hospital policies, etc.)

Example Structure of a Practice Lease Arrangement

Acquire Assets and Enter PSA

- Hospital purchases assets from group practice at fair market value
  - Hospital provides the purchased space and equipment back to the group practice for use by the physicians
- Support staff employed by hospital; APCs stay with the group practice
- Physicians and APCs employed by Group
- Hospital bills and collects
- Hospital leases professional services from Group
  - Usually a per WRVU rate
  - Hospital pays for provider benefits and malpractice at cost

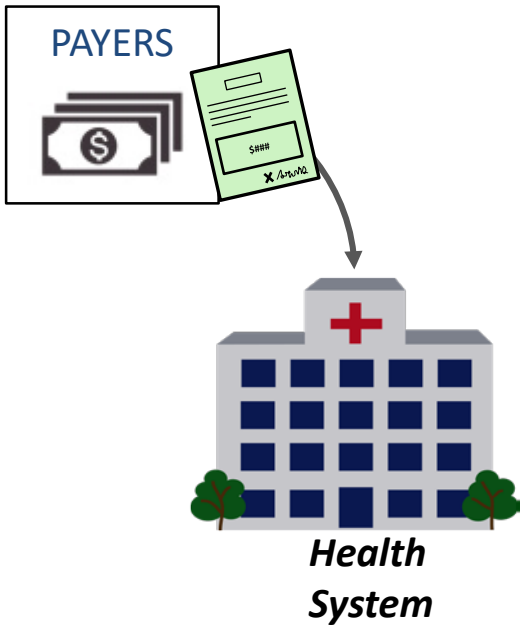
Example Compensation Under PSA/Lease Model



Acquire Equipment; Enter PSA and MSA

- Hospital purchases identified equipment from group practice at fair market value
  - Hospital provides the purchased space and equipment back to the group practice for use by the physicians
- Support staff and ACPs stay employed by the group
- Physicians and APCs stay employed by Group
- Hospital bills and collects
- Hospital leases professional services from Group
  - Usually a per WRVU rate
- Hospital leases identified resources
  - Payment based on budgeted annual cost plus a percent mark-up

Example Structure of Lease with Professional and Management Services Arrangements



Hospital assumes payer contracting role;
maintains payer contracts;
bills/ collects for services;
assumes related reimbursement risks.

Example Structure of Lease with Professional and Management Services Arrangements

Example Structure of Lease with Professional and Management Services Arrangements

Hospital maintains payer contracts and bills/ collects for services

Health System

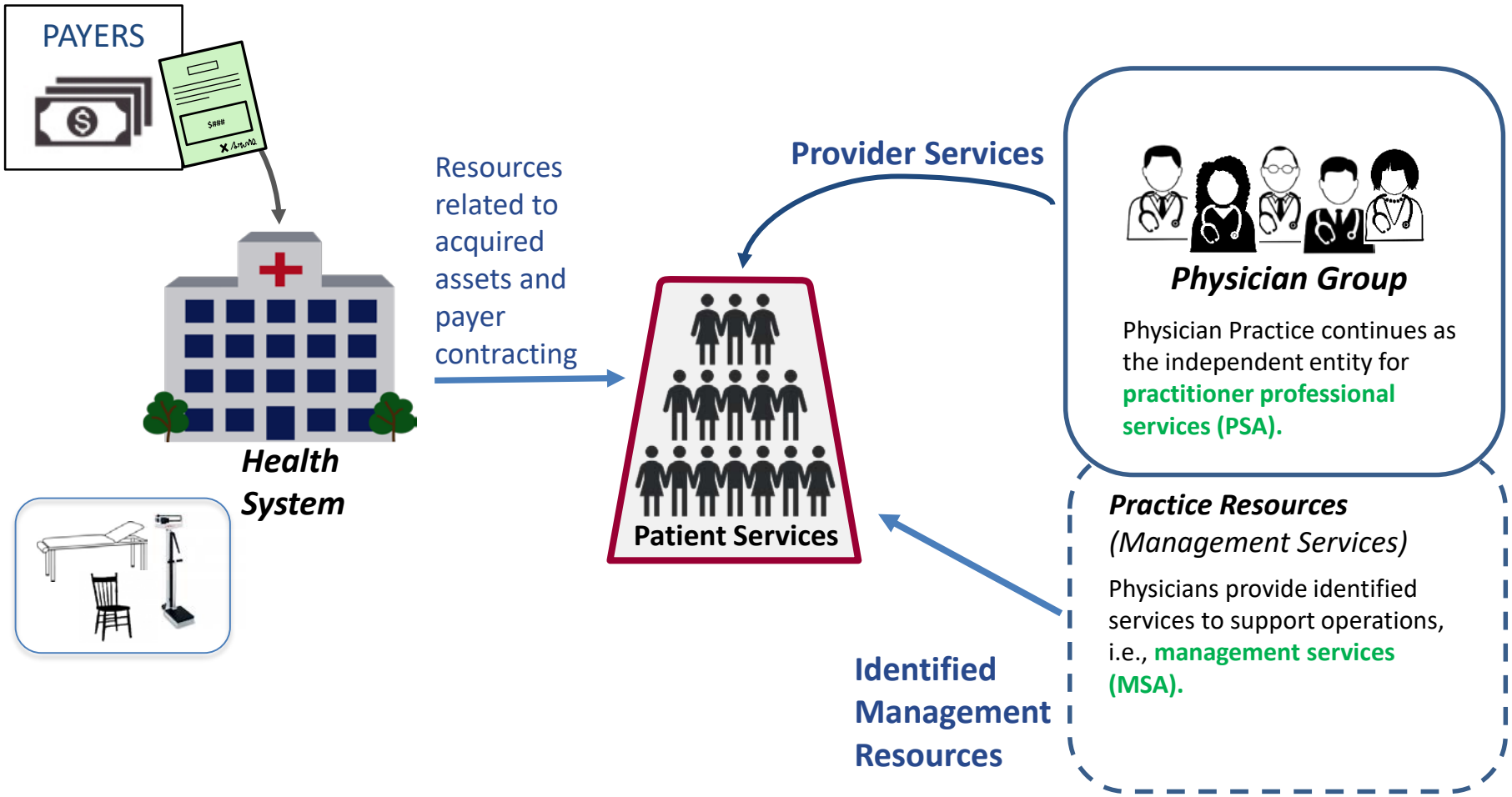
Physician Group

Physician Practice continues as the independent entity with employed providers.

Practice Resources *(Management Services)*

Physician group retains support staff, facility management responsibilities, and other operational functions.

Example Structure of Lease with Professional and Management Services Arrangements



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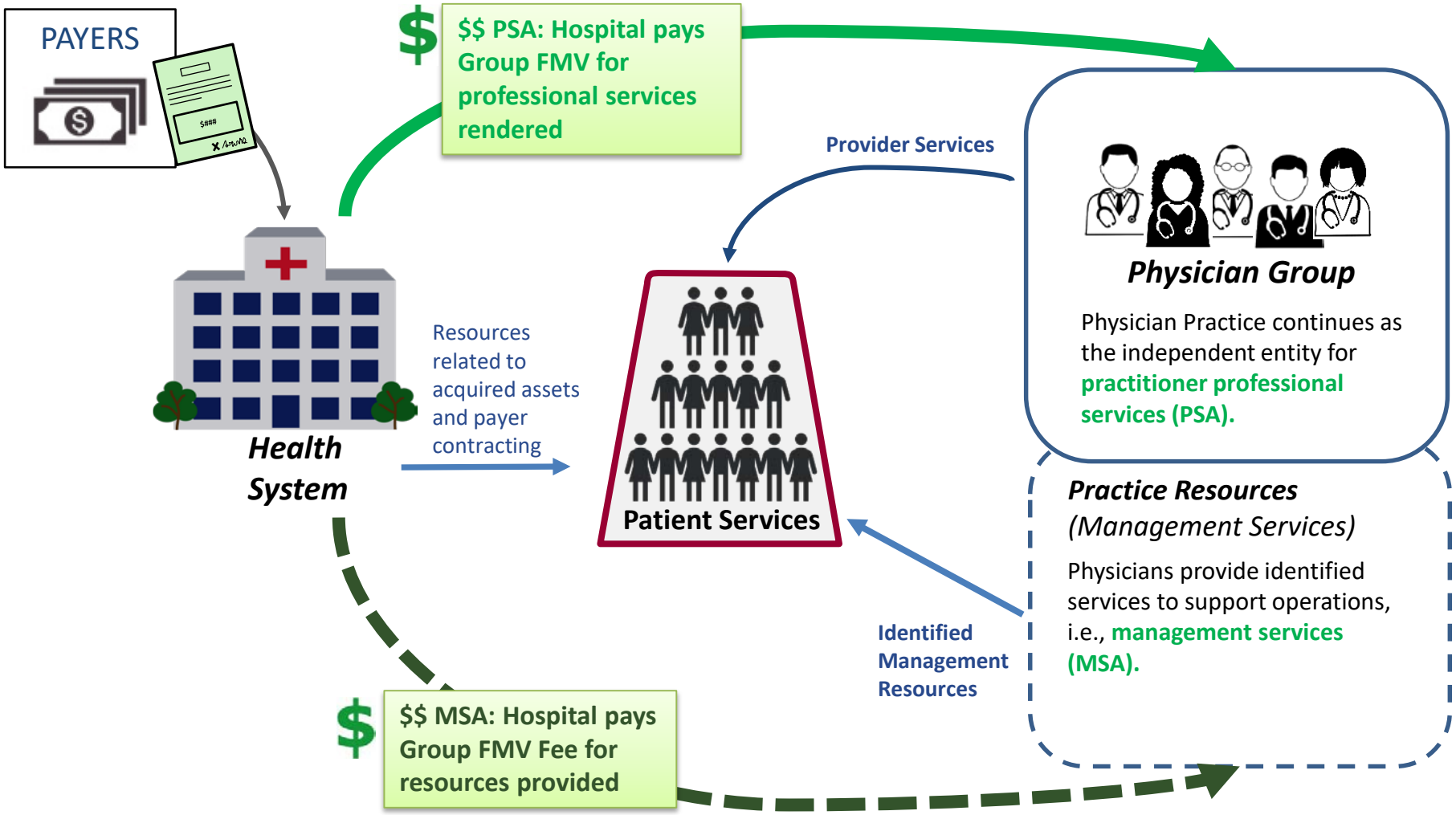

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Legal and Fair Market Value Considerations

PSA Legal Considerations: Stark Law

42 U.S. Code § 1395nn -- Physician may not refer patient to a hospital with which the physician has a direct or indirect compensation arrangement (unless an exception applies).

- Stark Law Exceptions generally require:
  - Contract in writing, signed by the parties, with term of at least 1 year
  - Services are reasonably and necessary for legitimate purposes of the arrangement
  - Compensation is set in advance, consistent with FMV
  - Compensation not determined in manner that takes into consideration value or volume of referrals or other business generated between the parties
- IOAS not applicable if Hospital is billing for services
- Proposed exceptions for “value based arrangements”

PSA Legal Considerations: Anti-kickback Statute

42 USC 1320a-7b – Prohibits knowingly and willfully offering, paying, soliciting or receiving any remuneration (anything of value, direct, indirect, overt or covert, in cash or in kind) to induce or in return for referring or arranging for any item or service payable by federal health care program.

PSA Legal Considerations: Anti-kickback Statute

Personal Services and Management Contracts Safe Harbor 42 CFR 1001.952 – Requirements:

- Written agreement signed by parties.
- Term of at least one year.
- Agreement must specify aggregate payment, and such payment must be set in advance. [OIG proposal: replace aggregate compensation with methodology.]
- Compensation must be commercially reasonable, fair market value and determined through arm's length negotiations.
- Agreement must set forth the exact services required to be performed.
- Compensation must not be determined in a manner that takes into account volume or value of referrals.
- All arrangements must be in ONE contract. There cannot be multiple overlapping contracts to circumvent the one-year rule.

* Proposed safe harbors for "value based arrangements"

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Managing Expectations

- Set expectations early.
- Make sure the physicians know what they can and cannot demand in negotiations.
- Stark Law exceptions available to group practice (IOAS) are no longer available under PSA model.
- Remember that Stark/AKS can be used as both shield and sword (and don't always take the bait).
- But do heed lessons learned from past settlements.

Fair Market Value Considerations

All assets and services of financial value exchanged between the hospital and physician must be compliant

- One Time Transaction/Payment
  - Purchase of assets
  - Purchase or sale of equity
  - Transfer of equipment
  - Sign-on or retention bonuses
  - One-time stipends
  - Malpractice tail coverage
- Ongoing Arrangement/Payments
  - Clinical and Administrative Services (Employment Arrangements)
  - Payment for other clinical services
  - Payment for other leadership and administrative services
  - Use of medical office space, work stations, medical or office equipment
  - Provision of EMR*, billing support services
  - Loans as compensation

FMV may serve as a ceiling or a floor for payment, depending on the nature of the transaction.

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Fair market Value Considerations: Management Services Arrangement

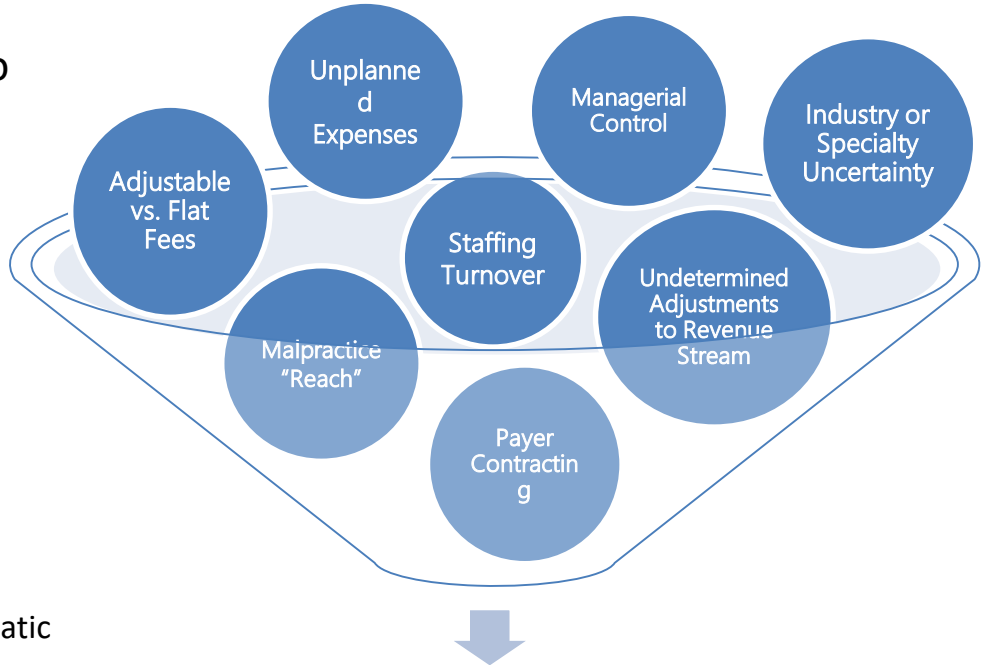
"What can we pay?" → "What are you paying for?"

- If you've seen one MSO – you've seen one MSO
  - Determining the components of the MSO is critical
  - The "Practice Resources" provided by the MSO and those resources provided directly by the hospital (e.g., billing, APCs)
  - Compare actual costs to market levels
  - Which party is responsible for the purchase of new equipment
  - Look out for "stacking" to avoid double-counting (i.e., paying twice)
- Method to determine (and change) the agreed-upon payment
- What if multiple entities are already established (Medical PC & MSO)
  - If multiple entities are already established, gather information from related entities
  - Review target practice resources in context of the whole
  - Determine whether current structure works, or if adjustments are required

Fair market Value Considerations:
Management Services Arrangement

"What can we pay?" & "What is comparable?"

- State fee splitting laws commonly prohibit "percent of revenue" based fees
- Comparable company operating margins reviewed to determine implied "mark-up" on costs
- Market data should be comparable to the services provided by the MSO
  - Staffing companies
  - Management companies
  - Other?
- Compensation structure and risk
  - Fixed fees and agreed-upon budgets are preferable
  - Risk for budgets not met
  - Reasonableness of the underlying costs
  - Only services provided are included
  - Per-WRVU payments are typically problematic
  - Non-compete provisions
- Early legal review and planning recommended



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Negotiations

PSA Negotiating Points

- Compensation
- Decision Making
- Real Estate
- Term & Termination
- Provider-based
- Equipment
- Unwind provisions

PSA Negotiating Points: Compensation

- Single payment to entire group
  - Must be FMV
  - Group may choose how to apportion across group members
  - Beware of indirect compensation (Stark Law)
  - Consider IOAS exception (Stark Law)
- wRVU productivity
- Third party payor contract incentive payments, clinical integration support funds, and at-risk reimbursement

PSA Negotiating Points: Decision Making

- Joint Operating Committee – members appointed by hospital and practice and decisions made jointly
  - Strategic planning and development
  - Participate in physician recruitment
  - Budgeting and capital requests
  - Practice standards and clinical protocols
- Decisions reserved to the hospital
- Decisions reserved to the practice

PSA Negotiating Points: Real Estate

- Physicians/practice retains ownership of office building and leases to hospital
- Hospital purchases building from practice
- Hospital subleases from practice

PSA Negotiating Points: Term & Termination

- Minimum term of three years
- Without cause termination only after initial term
- For cause termination

PSA Negotiating Points: Provider - Based

- Physician services and practice ancillaries will be billed by hospital either provider-based or free-standing
  - 2015 Site Neutrality eliminated most new off-campus provider based beginning in 2017
- 340b Drug Pricing only available if site of service meets provider-based status standards

PSA Negotiating Points: Equipment

- Physicians may own equipment and lease it to hospital
  - Who pays maintenance and replacement costs?
- Physicians may sell equipment to hospital for a one-time lump some payment

PSA Negotiating Points: Unwind Provisions

- Upon termination, practice needs to recoup:
  - Office space
  - Personnel
  - Revenue cycle management
  - Medical records custody
  - Access to vendor contracts necessary to operate practice
  - New payor contracts

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Questions?

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