Stark Law - Lessons Learned from Settlements in Whistleblower Cases

As settlements from whistleblower cases are negotiated, the False Claims Act and the Physician Self-Referral Law or “Stark” continues to define the landscape for physician compensation. Stark prohibits physician self-referrals of designated health services for Medicare and Medicaid. Stark was primarily developed to curtail improper financial incentives that are seen to increase healthcare costs related to the Medicare program and its beneficiaries.

Observers of key trends in the healthcare industry have watched with interest as the recent settlements with three medical service providers began to take shape. The cases involving Halifax Hospital of Daytona (Fla.), Infirmary Health of Mobile (Ala.) and the New York Heart Center are prime examples in which healthcare providers – rather than face further legal scrutiny over alleged Stark Law violations — chose to enter into monetary damages agreements, paying to resolve or settle pending action that included the potential for sizable fines. In the Halifax case for instance, the settlement reached was for a reported $85 million, but, according media reports, Halifax was facing possible fines exceeding $1.1 billion if a Stark violation decision had been reached by the court.

A focal point in all three cases centered on the question of whether or not the hospitals paid physicians more than fair-market value and whether or not the payment was commercially reasonable. In these cases, the Bona Fide Employment Exception became a key issue and a point of debate. Under this exception, money paid to doctors is not considered compensation subject to the Stark Law as long as the doctors receive no more than fair-market value for the services. In addition, under the Bona Fide Employment Exception, payments to doctors do not vary with the volume or value of the services performed through the hospital.

Yet, as a common thread in each of these three cases, it was alleged that the physicians involved in the Stark action were compensated based on formulas that take into account the volume of referrals. Following the adoption of Stark, it became imperative that compensation between the hospital and physician should be an arm’s length transaction. In addition to remaining within fair-market value, compensation must be commercially reasonable and it should not take into account the volume or value of referrals. To maintain compliance with Stark, there must also be a legitimate business purpose whereby the hospital needs the service.

Key Compensation Issues in Halifax Case

In the Halifax case, there were two primary physician agreements in question. In the first contract, the court held that a bonus pool consisting of a percentage of net profit from the physicians’ medical oncology service line at the hospital took into account the volume or value of their referrals in violation of federal law.[1] Halifax entered into employment agreements with six oncologists that incorporated a bonus compensation pool comprised of 15 percent of the operating margin of the whole hospital medical oncology program. Historically, there have been vehicles (i.e. co-management agreements) for sharing savings with very tight restrictions on the type of savings and how they are measured, particularly with Medicare. However none of these would have included a percentage of the net profit, as net profit is a function of total revenues which are directly impacted by volume less total expenses, at least some of which would be fixed, depending on the definition.
The hospital admitted that the compensation pool included revenues for all services performed in the oncology practice. Halifax compensated the oncologists identified in the case based on operating margins of the group as a whole as opposed to what they personally produced.

In the second contract, Halifax also had to contend with commercial reasonableness issues related to contracts it had established with some of its neurosurgeons on staff. When compared against the Stark Law, the employment agreements for the neurosurgeons in question were not considered commercially reasonable because there did not appear to be a legitimate business purpose for entering into or maintaining the employment agreements — other than the physician referrals.

The commercial reasonableness issues focused on the following key points:

- The neurosurgeons in the case received favorable treatment in the form of car allowances and additional subsidies that were not provided to other physicians, including not deducting collections and bad debt from collections. Per the Order on the Motion for Summary Judgment,[1] the neurosurgeons were essentially “allowed to operate their practice with a guaranteed salary and keep 100% of their collections with no overhead expense.”
- Additional areas of concern included inflation of productivity numbers and paying the physicians higher than the 90th percentile despite collections being lower than that percentile. With the exception of the oncologists, the neurosurgeons were the only other specialty group that was paid above or near the 90th percentile.

In addition to the bonus pool and the commercial reasonableness issues, the Stark investigation and proceedings addressed Halifax’s approach to hospital’s wRVU calculations. Ultimately the court denied the order for summary judgment indicating that “the propriety of the neurosurgeons’ compensation under the Stark Act is a matter for a jury to decide.”

While the lessons taken from the Halifax case are numerous, the Stark action highlighted the need to review compensation arrangements to ensure that the volume of referrals is not included. It also underscored the importance of hiring qualified valuation professionals to determine the fair market value of employment agreements. In the case of Halifax, if the neurosurgeons were paid in excess of fair-market value for their services, the agreements do not make commercial sense and they would not have been entered into by a reasonable entity of similar size and type.

**False Claims: Central Issue in Stark Cases of Mobile Infirmary & New York Heart Center**

In reviewing the Stark Law violations brought against the Mobile Infirmary and the New York Heart Center, the government, alerted from tips provided by whistleblowers, pursued legal action because it found that compensation was not at fair-market value or commercially reasonable. The false claims charge was also the result of the volume or value or other business generated by the referring physician.

Mobile Infirmary did not admit to any wrongdoing as part of the settlement reached with federal prosecutors. However, the hospital agreed to pay $24.5 to settle the case, with $4.41 million going to the whistleblower who called the Stark violations to the government’s attention.

With the case brought against the Mobile Infirmary, the government alleged that the physicians overused cardiology imaging with nuclear stress tests and the doctors were financially rewarded for
ordering more tests. According to the complaint, Mobile Infirmary physicians altered records and falsely claimed that patients had chest pains so that they could order the tests.

The government investigation of the Mobile Infirmary further found that the health system provided favorable treatment to the physicians in the form of reduced rents at below market rates. The case against the Mobile Infirmary also alleged that incentive bonuses for the physicians involved were based on the margins of the group rather than the actual physician compensation, which can be varied based on referrals for designated health services. Another serious false claims charge in this case involved the discovery of secret payouts from the fees from government health programs to physicians – payments which were held back by one year and disguised so that there was not a direct correlation to the physician’s productivity.

In the New York Heart Center case, referrals were also at the center of the false claims Stark prosecution brought against the hospital. Following up on a whistleblower tip, the government alleged that partner physician compensation rates were based on a formula that took into account the volume of referrals for nuclear and CT scans. Rather than utilizing a compensation model based on each physician’s productivity, New York Heart Center placed a significant focus on rewarding physicians for the number of referrals made – a practice which is not allowed under Stark. Even though the New York Heart Center did not admit guilt, they agreed to pay a $1.34 million settlement to avoid prosecution on the Stark violations.

We Can Help!

In light of the Stark Law and other changes in the healthcare industry, maintaining compliance with physician compensation regulations has become more complex for hospitals and healthcare providers. Review of physician compensation is best done with a team that includes a healthcare attorney, healthcare valuation/accounting professionals and hospital leadership that understands the workings of the practice. Particularly in the review of existing relationships, the first step may be a consultation with a healthcare attorney. If your hospital has questions concerning Stark compliance or other administrative healthcare regulations, please contact the Elliott Davis Decosimo Healthcare Team at 866-417-4059.

Nicole Gossett, CVA is a manager at Elliott Davis Decosimo. She may be reached atnicole.gossett@elliottdavis.com

H. Kennedy Conner, CPA, is a shareholder at Elliott Davis Decosimo. He may be reached atken.conner@elliottdavis.com