Federal District Court Opinion May Have Crippling Impact on Physician-Hospital Relationships

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An as-yet unpublished ruling issued last fall by a Federal District Court Judge in the Western District of Pennsylvania could have far-reaching effects on physician-hospital relationships around the country.

In *United States ex rel. Singh, et al. v. Bradford Medical Center et al.*, the Court found that a hospital violated the Stark II law by submitting claims to Medicare based upon referrals from physicians with whom the hospital had a financial relationship. Additionally, the Court held that a jury will need to decide if the relationship also violated the anti-kickback statute, which prohibits hospitals from paying physicians for Medicare referrals.

Background

Two internal medicine physicians had been sending all of their cardiac imaging cases to Bradford Regional Medical Center, an acute care hospital located in Bradford, PA, representing 42% of all of the hospital's referrals for such imaging services. Rather than continuing to send patients to the hospital, the doctors decided to lease a nuclear camera from General Electric and operate the facility themselves. In response, the hospital adopted an "economic credentialing" policy so that the staff privileges of any physician who competed with the hospital would not be renewed.

After much negotiation, the doctors agreed to sublease the nuclear camera to the hospital for rental payments equal to those the doctors were paying to GE. They also agreed not to compete with the hospital within a 30 mile radius. The hospital paid the doctors $23,000 per month for the non-compete, $2,500 per month for the use of office space (with no written lease), and a "billing and collection fee" equal to 10% of all revenue.

The hospital engaged its accountant to determine the fair market value of the non-compete payment. His analysis - which the doctors never even saw - was based on the assumption that, because of the non-compete, the doctors would refer all their imaging to the hospital "even though they were not required to do so." In addition, the hospital CEO submitted a report to his board claiming that the hospital expected to generate $402,000 in profit from the additional nuclear imaging referrals it anticipated to be generated by the doctors after entering into the transaction, again making clear that the hospital entered into the negotiated settlement with the anticipation of receiving referrals.

The Ruling

The lawsuit contended, and the judge agreed, that the arrangement was not a bona fide sublease of equipment needed by the hospital, but a disguised attempt to pay the doctors for referrals. The judge held that as a matter of law, Stark II was violated because the remuneration paid by the hospital to the physician group "took into account" the value or volume of anticipated referrals from the physicians to the hospital.

The judge acknowledged that the doctors and the hospital negotiated the compensation arrangement in an arm's length fashion and that the value to the doctors of getting out of the nuclear imaging business was roughly equal to the stream of income that they were giving up. However, he said that is not the definition of "fair market value" for purposes of Stark II. He pointed to language in the regulations that defines "fair market value" of a compensation arrangement as the "*result of bona fide bargaining between well-informed parties to the agreement who are not otherwise in a position to generate business for the other party . . . where price or compensation has not been determined in any manner that takes into account the volume or value of anticipated or actual referrals.*" Since the compensation arrangement here was with a party who was in a position to refer business to the hospital and unquestionably "took into account" anticipated referrals, it was not "fair market value" as defined in Stark II. Hence, the arrangement violated the law.

Significance

The facts of this case do seem quite troubling from the perspective of the Stark II statute. At the same time, the language of the judge's opinion is broad enough to implicate many other financial relationships between hospitals and physicians because it is likely that most of these relationships "take into account" anticipated referrals in one form or another. For example, when a hospital employs a physician, it almost certainly has in mind the physician's ability to utilize hospital services such as imaging by way of referrals. Has the hospital just violated Federal law by "taking into account" these referrals in setting the physician's compensation?

As of today, the decision by the District Court Judge has formal precedential value only in the Western District of Pennsylvania. If the case is not resolved it will likely be appealed, however, giving an appellate court the opportunity to consider the matter.

Physicians should also be aware that this case was not initiated by the government, but rather by private parties, perhaps competitors of the doctors involved. Hence, before entering into any arrangement that could potentially implicate the self-referral laws, both Federal and State, physicians should assume that the arrangement will be scrutinized.

If you have questions or would like more information, please contact any member of the Healthcare Practice Group at Flaster Greenberg PC.

ATTORNEYS MENTIONED

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