

HEALTH CARE LAW UPDATE

July 2007

Hospital Law Issues

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OIG Disapproves Partial Sale of Physician ASC Interest to Hospital

The Office of Inspector General of the U.S. Department of Health and Human Services (“OIG”) recently released an advisory opinion concluding that the proposed sale of ownership interests by physician owners of an ambulatory surgical center (ASC) to a hospital posed compliance issues under the federal Anti-Kickback Statute.

The Facts

The ASC is owned by three orthopedic surgeons (who together owned a 94% interest) and two gastroenterologists and two anesthesiologists (who together owned a 6% interest). The three orthopedic surgeons proposed selling 40% of their ownership interests to a nearby hospital for cash. The amount paid by the hospital would be fair market value, but it would exceed the amount originally invested by the orthopedic surgeons (the “founding members”) for their interests in the ASC.

The orthopedic surgeons did not offer to sell their interests to anyone else other than the hospital and the gastroenterologists and anesthesiologists did not offer to sell any portion of their interests to the hospital.

Because the hospital is in a position to make or influence referrals to the ASC and its physician owners, it agreed to adopt certain safeguards (identified in prior OIG advisory opinions) such as prohibiting its employed physicians from making referrals to the ASC; not taking any actions to require or encourage its medical staff to make referrals to the ASC, and not tracking any such referrals.

All compensation paid to physicians affiliated with the hospital would be fair market value and not take into account referrals to the ASC. The hospital would notify its medical staff of these measures and would continue to provide outpatient surgical services at its own facilities.

The OIG’s Analysis

The OIG started its analysis by pointing out its long-standing concern about certain suspect contractual joint ventures, such as ASCs owned by physicians and hospitals. It noted that these ventures have the potential to pose a risk that income from the venture may constitute payments for referrals to the ASC or to co-investors.

According to the OIG, the proposed arrangement would not qualify for safe harbor treatment under the hospital-physician ASC safe harbor because the amount of payment to an investor in return for the investment would not be directly proportional to the amount of capital invested by that investor in the ASC.

The OIG concluded that the proposed arrangement posed a heightened risk of fraud and abuse for the following three reasons:

1. The hospital would purchase its 40% ownership interest directly from the orthopedic surgeons for cash, rather than make a capital contribution to the ASC itself. Thus, the hospital’s investment would not result in an expansion or enhancement of the ASC, but, instead, the orthopedic surgeons would realize a

gain on their original investment in the Company.

2. Not all of the physician owners would sell a portion of their ownership units to the hospital for an appreciated price. Thus, there was a possibility that one purpose of the hospital's investment was to reward a subset of physician owners (the orthopedic surgeons) for their valuable referrals of patients to the hospital or the ASC.

3. Because the hospital was paying a higher price for its 40% interest than what the physician investors initially paid for their interests, the return on the investment would not be directly proportional to the amount of capital invested by each investor. Thus, although distributions of profits and losses would be made in proportion to the investors' ownership interests, the hospital would, in effect, pay more per ownership unit than what the orthopedic surgeons paid; consequently, the orthopedic surgeons would receive a higher rate of return on their remaining ownership interests than the hospital would receive on its newly-acquired interest.

Conclusion

The OIG noted that none of the above factors, standing alone or in combination, necessarily indicates fraud or abuse. Interestingly, the OIG attached little significance to certain fundamental factors that it has focused on in prior advisory opinions. For example, the fact that the hospital's purchase price was certified to be fair market value did not seem to bear much weight with the OIG. Similarly, the fact that the hospital would adopt certain safeguards (which the OIG has blessed in prior advisory opinions) did not hold much sway with the OIG.

Further, various, seemingly widely-accepted aspects of the proposed arrangement, appeared to be problematic. For example, the OIG failed to differentiate its position from its past opinions in which it approved arrangements involving distributions of profits and losses in proportion to ownership interests.

In at least in one prior opinion, the OIG approved an arrangement in which a hospital purchased its interest in an ASC for a higher price than the price paid by certain founding physicians; the differential, it explained, was the result of appreciation in the value of the ASC over time. By now focusing on the rate of return of the investment (versus a return proportionate to ownership), the OIG would make it almost impossible for a hospital to purchase a portion of a physician's ASC interest if the interest has appreciated in value.

In sum, although advisory opinions in general provide valuable insight on what the OIG considers permissible and not permissible, it is important to keep in mind that advisory opinions are limited to the facts of the particular case. Although it is not clear, the OIG may have reached a different conclusion in this case if certain aspects of the arrangement were different -- for example, if the hospital paid its buy-in to the ASC and thus directly funded the ASC's expansion or operations, or if the hospital's purchase price was based on the same fair market value methodology used to compute the buy-in price of the gastroenterologists and anesthesiologists (who were not "founding members" of the ASC).

In conclusion, this advisory opinion suggests that the OIG will subject purchases by hospitals of physician interests in ASCs (and maybe other types of health care services also) to heightened scrutiny, especially if the hospital is buying a partial interest from a subset of physicians for a higher price than the acquisition cost to the physicians. Thus, hospitals should use extreme caution in any transaction involving the purchase of a physician's interest in any venture.

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One Rockefeller Plaza
New York, NY 10020
Tel: (212) 643-7000
Fax: (212) 643-6500

The Legal Center
One Riverfront Plaza
Newark, NJ 07102
Tel: (973) 643-7000
Fax: (973) 643-6500

650 College Road East
Princeton, NJ 08540
Tel: (609) 227-4600
Fax: (609) 227-4646

www.sillscummis.com

Sills Cummis Epstein & Gross P.C.

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