

Negotiation of a Hospital-Based Physician Exclusive Contract

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Overview of Exclusive Contracting for Physicians and Hospitals

Benefits of Exclusive Contracting for Physicians and Hospitals

- Enhances patient care;
- The assumption by Group of responsibility for effective administration, supervision and coverage;
- The development of necessary working relationships between the Group and other hospital personnel and departments;

Benefits of Exclusive Contracting for Physicians and Hospitals (Cont'd.)

- Aids in obtaining continuous supervision, training, administration, scheduling and coverage;
- Hospital control over operation of its department;
- Assures full-time availability of services;
- Lowers costs through standardization of procedures and centralized administration of the departments;

Benefits of Exclusive Contracting for Physicians and Hospitals (Cont'd.)

- Allows better scheduling of the use of the facilities;
- Facilitates maintenance of equipment;
- Improves supervision of the support staff and working relations between staff and physicians;
- Assures that physicians perform sufficient procedures to maintain and upgrade their skills and maintain high standards of professional quality of care;

Benefits of Exclusive Contracting for Physicians and Hospitals (Cont'd.)

- Assures of the most effective and efficient teaching services for the benefit of the patients, medical staff and other appropriate personnel; and
- Assures compliance with the accreditation and licensing requirements.

Trends in Exclusive Contracting

- Exclusive arrangements are common place among the traditional hospital- based specialties. Examples include:
 - Anesthesiologists;
 - Radiologists;
 - Emergency room physicians; and
 - Pathologists.
- Specialists such as neonatologists, surgeons and neurosurgeons are increasingly entering into exclusive arrangements with hospitals.

Critical Legal Issues to be
Considered in all Exclusive
Hospital Contracts

State Law, Anti-Trust & Other Legal Challenges to Exclusive Contracting

1. Check state law to see if exclusive contracts are permitted.
2. If granting exclusive privileges, check hospital bylaws and/or state law to determine how to address physicians currently on staff.

State Law, Anti-Trust and Other Legal Challenges to Exclusive Contracting (Cont'd.)

3. What claims may a physician assert after he/she is excluded from a Hospital staff due to the granting of an exclusive contract?
 - That the exclusive contract violates federal or state antitrust laws.
 - That the exclusive contract violates constitutional due process protections.
 - That the exclusive contract constitutes the prohibited corporate practice of medicine

Considerations for Tax-Exempt Hospitals

- The impact of an exclusive contract on a hospital's tax-exempt status must be considered.
- Under the Internal Revenue Code and IRS regulations, a tax-exempt hospital must be organized and operated exclusively for an exempt purpose.

Considerations for Tax-Exempt Hospitals (Cont'd.)

1. Private Inurement

- No part of the hospital's net earnings may inure to the benefit of private individuals (“insiders”).
- Insiders may include physicians on a hospital's medical staff if the facts and circumstances tend to show substantial influence by the physician over the hospital.
- If any compensation is given under an exclusive contract, to avoid private inurement concerns, it must be reasonable and the result of arms-length bargaining.

Considerations for Tax-Exempt Hospitals (Cont'd.)

2. Private Benefit

- The hospital must be operated for public benefit, rather than for the benefit of any private interest.
- Private benefits is permissible only if it is incidental to effecting an exempt purpose.
- To avoid a violation of the private benefit prohibition, physician services under an exclusive must be necessary for the Hospital to pursue its charitable activities and the amount paid must be reasonable for the services actually rendered.

Excess Benefit Transaction / Intermediate Sanctions

- Intermediate sanctions may be imposed for transactions between a tax-exempt organization and persons who can exert substantial influence over the organization (a “disqualified person”) in situations where the transaction results in excess benefit.
- These sanctions are deemed intermediate because they lie between taking no action and revoking an organization's tax-exempt status

Excess Benefit Transaction / Intermediate Sanctions (Cont'd.)

- Some Group physicians may meet the definition of “disqualified person” for purposes of the intermediate sanction rules.
- Whether an excess benefit is provided turns on whether the value of the economic benefit provided by the hospital exceeds the value of the consideration (including performance of services) received by the Hospital

Private Use Considerations

- The private use of property financed with tax-exempt bonds may result in private business use which implicates certain requirements for contractual relationships between the private interest using or benefiting by use of the property and the owner of the bond-financed property.
- In determining whether an exclusive contract could raise private business use concerns, follow Internal Revenue guidance (Rev. Proc. 97-13; Rev. Proc. 2001-39).

Federal Fraud and Abuse Concerns

Anti-Kickback Law

- 42 U.S.C. § 1320A-7b(b) prohibits the payment of an "inducement" (anything of value) for the referral of Medicare and Medicaid business. This prohibits both the solicitation or receipt of the inducement, as well as the offer or payment.

Anti-Kickback Law (Cont'd.)

- Any compensation paid by the Hospital to the physician group under the contract (e.g. medical director fees) can not be intended as an inducement for the physician members of the physician group to refer patients to the Hospital.
- If feasible, structure the exclusive contract to comply with the personal services safe harbor.

Stark Law

- The Federal physician self-referral law (the “Stark Law”) prohibits a physician from referring patients to entities with which he/she has a financial relationship for the provision of designated health services ("DHS") reimbursable by a federal health care program, unless an exception to the Stark Law applies.

Stark Law (Cont'd.)

- Because an exclusive contract would be with a physician group rather than with its physician members, the Stark Law requires a determination whether the direct financial relationship created between the hospital and the physician group by the exclusive contract would result in an indirect financial relationship between the physician members of the Group and the Hospital.

Stark Law (Cont'd.)

- If such an indirect financial relationship is present, a determination must then be made whether the exclusive contract satisfies the requirements of an exception to the Stark Law for indirect compensation arrangements.

Careful Drafting of Exclusive Contracts is Important

Common drafting errors include:

- Proper legal name for both parties is not included.
- Defined contract terms are used consistently.
- Section numbers referred to incorrectly.
- Remember which side you represent.
- Don't rely on exhibits and schedules prepared by your client.

Factual Background for
Negotiation of Exclusive
Radiology Services Agreement

Factual Background

- Memorial Hospital (“Hospital”)
 - 250 bed Community Hospital
 - Wants to expand its radiology service
- Radiology Associates (“Group”)
 - Sole Radiology service provider at Hospital for past 15 years
 - Also performs reads for local multi-specialty groups

Factual Background (Cont'd)

- Group uses office space at Hospital
- Dr. May is President of Group & Hospital Med Staff
- Group has experienced difficulty obtaining adequate professional insurance coverage
- Hospital cardiologists concerned about possible exclusive arrangement with Group

Factual Background (Cont'd)

- Exclusive offer does not include MRI reads
- Ancillary personnel to be employed by Hospital
- Hospital wants to assume billing for Group
- Hospital will require round-the-clock on-site coverage

