Crowell

CLIENT ALERT

Landmark False Claims Act Judgment: What Hospitals and Healthcare Providers Should Know

October 17, 2013

On October 2, 2013, the federal district court in Columbia, South Carolina imposed a landmark $237 million judgment in a much-discussed False Claims Act case which was predicated on violations of the Physician Self-Referral (Stark) Law, *U.S. ex rel. Drakeford v. Tuomey Healthcare System, Inc*.[1] The case was originally filed as a *qui tam* case in 2005 by a physician, Michael Drakeford. The federal government intervened in the case in 2007.

The relator Drakeford and the government alleged that Tuomey Healthcare System (Tuomey) had established employment relationships with certain referring physicians which did not meet a Stark Law "exception," thus tainting all Medicare referrals and claims submitted by Tuomey for services resulting from these physicians' referrals. The physicians, employed through Tuomey's affiliated medical practice groups, were part-time employees and their compensation covered only the physicians' outpatient surgery services. The physicians' salaries were adjusted according to collections received by the hospital for the services personally performed by the physicians. The physicians also received productivity and quality bonuses based on a percentage of these collections.

The government presented testimony that leading up to the employment of these physicians, Tuomey had calculated the fees it would lose if the physicians were to perform their surgeries at a competitor ambulatory surgery center. There was evidence that Tuomey also determined that even though the physicians' compensation would exceed Tuomey's collections from the physicians' personally performed services, the employment relationships were nonetheless valuable to Tuomey.

The government argued in part based on this evidence, that the physicians' aggregate compensation "varied with, or took into account the volume or value of referrals or other business generated" by the physicians for Tuomey, and therefore constituted an "indirect compensation arrangement" between the physicians and Tuomey. The government argued specifically that Tuomey's facility fees constituted the physicians' referrals and that their compensation, which fluctuated directly on the basis of the physicians' personally-performed physician fees, also fluctuated consistently with those "facility fee" referrals. The government further argued that the arrangements did not meet the indirect compensation arrangements exception because the compensation "took into account the volume or value of referrals or other business generated" by the physicians for Tuomey,[2] was not consistent with fair market value and was not commercially reasonable unless the physicians made referrals to Tuomey.

When the case was first tried in federal court in 2010, the jury concluded, based on this theory, that Tuomey had violated the Stark Law, but found rather surprisingly that it *had not* violated the False Claims Act. The federal district judge set aside the jury verdict and entered judgment for the government, but only on the government's equitable claims, not its FCA claims. Tuomey and the government cross-appealed this decision to the Fourth Circuit which reversed the decision below on March 30, 2012, based on Seventh Amendment grounds irrelevant to the Stark Law. However, the Fourth Circuit also offered "advisory guidance" with respect to the applicability of the Stark Law to certain issues in the case. The advice was confusing to many, and so issues lingered following the decision with regard to how key Stark Law phrases such as "volume or value of referrals," "commercial

reasonableness" and "fair market value" were interpreted. Confusion also arose as to whether only an agreement's "four corners" were to be considered, rather than all the evidence, in so determining.

With this "advice," following re-trial in the spring of 2013, the jury concluded that Tuomey *had* violated the Stark Law *and* False Claims Act, and that Tuomey had submitted a total of 21,730 false claims valuing $39.3M in payments.

On September 30, Judge Margaret B. Seymour denied a series of Tuomey's post-trial motions, determining instead that a reasonable jury could have found that the physicians' employment compensation did "vary" with referrals – even though physician compensation was not expressly connected to those referrals – because Tuomey also received a facility fee each time one of the physicians personally performed a procedure at the hospital, which the court characterized as evidence of a "one-to-one relationship" between the physicians' aggregate compensation and the physicians' referrals. Judge Seymour also found that a reasonable jury could have found that Tuomey "took into account" the volume or value of referrals in "establishing the physicians' compensation." The court entered judgment under the False Claims Act at approximately $237.5 million, including treble damages and civil penalties.[1]

ANALYSIS

While the September 30 ruling was, in effect, a "sufficiency of the evidence" finding, this case, its facts, and its tortured court proceedings, provide valuable lessons while raising perplexing questions for hospitals and other health care providers as to the establishment of compensation arrangements with physicians. These new complexities come at a time when the Affordable Care Act and other economic factors are encouraging broader physician integration with these providers. As health care delivery systems react to this changing landscape in part through tighter financial affiliations with physicians, the analytical and practical ramifications of Tuomey must be addressed:

1) The Accumulation of "Bad Facts" May Matter in a Stark Law "Analysis." This case involved a series of unique facts concerning the physician compensation relationship that we believe in combination may have "tipped" the Stark Law analysis against Tuomey for the prosecution.

- The employed physicians had been in the process of establishing a competitor ASC to Tuomey when they were approached for employment. Some evidence did indicate that the hospital, before entering into the physician employment relationships, had calculated the referrals it would have lost if the physicians performed procedures at non-Tuomey facilities.
- The employment agreements were only part-time arrangements. At all other times, the physicians worked independently from the hospital, including operating their own independent group practice.
- Tuomey recognized that the physicians' compensation would be higher than the fees collected for their individually-performed services.

2) Obtaining a Fair Market Value Assessment Remains Vital to Achieving Stark Compliance. While the Stark law does not require an independent evaluation to determine if compensation comprises fair market value, it is always best practice to obtain such an evaluation prior to making hiring decisions.

3) Commercial Reasonableness Remains A Confusing Concept. Despite judicial (and prosecutorial) confusion, assessments of the reasonableness of entering into a physician compensation arrangement or acquisition may include determinations of the impact a group acquisition or employment may have on, e.g., a hospital system. However, those commercial assessments ought not be utilized in identifying fair market value or setting compensation.

4) "Financial Losses" Are Not Per Se Stark Violations. Operating a physician group at a financial "loss" is not per se illegal. However, this circumstance places more pressure on the employer entity to justify the fair market value of the compensation to be paid, as well as the absence of any "volume or value of referrals" assessment, as a counterweight to the losses.

5) The Government Is Willing to Enforce the Stark Law. Even when the facts are complex and the Anti-Kickback statute is not an available enforcement alternative, we have seen an increasing number of Stark Law *qui tam* actions, and the government's interests therein. As noted, the confusing Fourth Circuit "advisory" decision in *Tuomey*, the case's complicated fact pattern, and now the exceedingly large damages award will only serve to fuel greater use of the complex and confusing Stark Law as a pathway to huge False Claims Act judgments or settlements. Providers should take the threat of Stark non-compliance quite seriously.

6) The Verdict and Fourth Circuit Court Decision Raise New Questions. The Stark law clearly permits physicians to be paid based on their "personally performed services." But when physicians are paid more than their employer's billings for these personally performed services does that mean these payments are not "commercially reasonable," that they must "vary with or take into account the volume or value of their referrals or other business generated between the parties" or that the compensation is not "fair market value"? May a designated health service entity such as a hospital deign to even consider whether a physician practice will operate in a gain or loss to the hospital before it is acquired? Thereafter, can a physician group which continuously operates at a loss remain within a Stark exception? Can there be legitimate "commercially reasonable" reasons for physicians to be paid more than their own billings? Can a physician be paid "fair market value," but fail the "commercially reasonable" requirement in such circumstances? These questions indicate that health care providers must proceed with even greater care in forming Stark-compliant physician financial relationships, at the precise point in time when healthcare reform serves to strongly encourage greater provider-physician integration.

---

[1] The court initially imposed a $277 million judgment on September 30, 2013, but reduced the judgment to $237 million on October 2, 2013.

[2] In order to effectuate an "indirect compensation arrangement," among other conditions, a physician's aggregate compensation must "vary with, or take into account the volume or value of referrals or other business generated by the referring physician for the entity furnishing DHS." *See* 42 C.F.R. § 411.354(c)(2). Similarly, in order to satisfy the indirect compensation arrangements exception, a physician's compensation must not be "determined in any manner that takes into account the volume or value of referrals or other business generated by the referring physician for the entity furnishing DHS," among other requirements. 42 C.F.R. § 411.357(p)(1). This seemingly impossible construct relies, in part, on special rules within the Stark Law regulations. If compensation satisfies each definitional element of an "indirect compensation arrangement," the compensation may satisfy certain special

rules that deem compensation not to "take into account the volume or value of referrals or other business generated," which do not apply at the definitional stage of analysis, but do apply at the exception stage. *See* 42 C.F.R. §§ 411.354(d)(2) and (3).

[3] Tuomey has since filed a notice of appeal with the Fourth Circuit.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

Troy A. Barsky
Partner & CHS Managing Director – Washington, D.C.
Phone: +1.202.624.2890
Email: tbarsky@crowell.com

John T. Brennan Jr.
Partner – Washington, D.C.
Phone: +1.202.624.2760
Email: jbrennan@crowell.com