



## Recent Stark Act decision could have significant impact for employed physicians compensated based on personal productivity

October 7, 2019

Update from February 11, 2020:

On December 20, 2019, the Third Circuit [vacated](#) its September 17, 2019, opinion and issued a [revised opinion](#). In the revised opinion, the Third Circuit deleted its entire controversial analysis regarding what it means for compensation to “vary with” the volume or value of referrals but, ultimately, still concluded that the whistleblower’s complaint plausibly pled that the compensation paid to employed surgeons took into account the volume or value of their referrals and was not consistent with fair market value. The revised opinion states:

We need not resolve the meaning of varies with here. Regardless, the complaint plausibly alleges that the surgeons’ compensation takes into account the volume or value of their referrals. Under the Stark Act and its regulations, compensation takes into account referrals if there is a causal relationship between the two. And here, the surgeons’ suspiciously high compensation suggests causation.

The deletion of the “varies with” discussion is a relief, as it removes the possibility of the government or a whistleblower pleading a Stark Law violation by simply alleging that surgeons and other physicians whose practices are hospital-based were paid based on their productivity for personally performed services. However, the revised decision is still potentially problematic, as well as inconsistent with language in the [CMS Proposed Rule published in October 2019](#). For example, CMS has [proposed](#) new definitions of commercially reasonable, fair market value and what it means to take into account the volume or value of referrals that should take much of the wind out of the sails of the Third Circuit’s decision. While this decision is an improvement over the

prior decision that could have wreaked havoc on health systems with employed surgeons paid based on their personal productivity, the revised decision is still controversial in many respects. CMS's Final Rule, expected out sometime in 2020, will reveal the final outcome on some of these issues.

Original post from October 7, 2019:

On September 17, 2019, the Third Circuit Court of Appeals issued a [decision](#) with potentially far-reaching consequences involving the Stark Act. The case, *United States ex rel. Bookwalter v. UPMC*, involves allegations that a compensation model for employed physicians, specifically surgeons, based on their productivity violated the Stark Act. In reversing the lower court's dismissal of the case and remanding the case back for further proceedings, the decision raises a number of issues for consideration, because it:

- calls into question very common physician compensation models that compensate physicians based on personal productivity
- makes it easier for whistleblowers to bring Stark Act-related False Claims Act cases involving physician compensation arrangements and survive motions to dismiss, significantly increasing defense costs
- states that the burden of proof in establishing the applicability of a Stark Act exception in False Claims Act cases is on the defendant, thus allowing the case to go to discovery without considering the applicability of various Stark exceptions

#### Background

The case focused on neurosurgeons who were employed through three subsidiaries of University of Pittsburgh Medical Center (UPMC). UPMC is the parent organization of a system of health care providers that includes 20 hospitals and subsidiaries through which the neurosurgeons are employed. The compensation model for the neurosurgeons included a base salary and an annual wRVU quota. If the neurosurgeons failed to meet their annual wRVU quotas, their employers could lower their future base salary. And if the neurosurgeons exceeded their quotas, they earned \$45 per wRVU above the quota threshold. Three whistleblowers (a neurosurgeon, a physician and an operating room technician) filed a qui tam lawsuit against UPMC and its subsidiaries alleging that the compensation arrangement with the neurosurgeons violated the Stark Act and the False Claims Act.

#### The allegations

The complaint alleges violations of the False Claims Act based on underlying violations of the Stark Act, including allegations that the aggregate compensation paid to the neurosurgeons exceeded fair market value based on the following: (1) at least some of the neurosurgeons' pay exceeded their collections; (2) many of the neurosurgeons' pay exceeded the 90<sup>th</sup> percentile for neurosurgeons nationwide (some were paid two to three times the 90<sup>th</sup> percentile); (3) many of the neurosurgeons generated wRVUs far above industry norms (most exceeded the 90<sup>th</sup> percentile by an "enormous margin," and some of the neurosurgeons seemed "super human," "racking up two to three times the 90<sup>th</sup> percentile;" (4) the neurosurgeons' bonus per wRVU exceeded what could be collected on most of those wRVUs, meaning that, according to the court, "the defendants took an immediate financial hit on [wRVUs] for a majority of their claims" which the court called "yet another sign that the surgeons' pay took referrals into account;" and (5) the government's prior settlement with UPMC and related entities (referenced below) included allegations that UPMC fraudulently inflated the neurosurgeons' wRVUs by (a) submitting claims for assisting with or supervising surgical procedures performed by other surgeons, residents, fellows or physician assistants when those neurosurgeons did not participate in the relevant surgeries to the degree required and (b) submitting claims to the Medicare program for levels of spinal decompression not actually performed. According to the court of appeals decision, "[t]hat much smoke makes fire plausible."

#### Procedural history of the case

The case was originally filed in 2012 by whistleblowers on behalf of the United States alleging that UPMC, University of Pittsburgh Physicians (one of the subsidiaries that employed most of the neurosurgeons), and a number of neurosurgeons submitted false claims to Medicare and Medicaid for physician and hospital services. In July 2016, the Department of Justice (DOJ) intervened in the case but only as to the claims related to the physician services and [settled](#) with UPMC and related parties for \$2.5 million. The government declined to intervene with respect to the claims related to the hospital services but, rather than seeking to dismiss the case, allowed the whistleblowers to proceed. The district court dismissed the remaining allegations without prejudice for

failure to state a claim. The whistleblowers refiled an amended complaint, which the district court dismissed with prejudice. The whistleblowers then appealed the dismissal to the Third Circuit Court of Appeals.

The Third Circuit reversed the dismissal and issued a decision that could have significant implications for health care providers that compensate physicians under a productivity-based model.

The Third Circuit's decision

The court articulated the three elements of a Stark Act violation:

1. A referral for designated health services (DHS)
2. A compensation arrangement (or an ownership/investment interest)
3. A Medicare claim for the referred service.

The court of appeals stated that “[w]hen they are all present, we let plaintiffs go to discovery.” In reversing the lower court’s dismissal of this case, the court of appeals agreed with the whistleblowers that all three elements had been plausibly pled in the complaint.

The court of appeals agreed there were referrals for DHS (specifically inpatient or outpatient hospital services), noting that “[e]very time [the neurosurgeons] performed a surgery or other procedure at the UPMC Hospitals, [they] made a referral for the associated hospital claims.” Thus, according to the whistleblowers’ complaint, as the neurosurgeons performed more procedures at the UPMC hospitals, those procedures required “the attendant hospital and ancillary services,” which the hospitals provided and billed Medicare for.

The court next examined the arrangements that the neurosurgeons have with the UPMC hospitals, noting that because the hospitals did not pay the surgeons directly, the initial question was whether there was an indirect compensation arrangement as defined under the Stark Act. The court concluded that the whistleblowers’ complaint “plausibly pleads enough facts to satisfy each element” of an indirect compensation arrangement, because it alleges that:

1. there was an unbroken chain of entities with financial relationships that connects the surgeons with the hospitals; UPMC owns each hospital, UPMC owns each UPMC subsidiary, and the UPMC subsidiaries employ and pay the surgeons.
2. the surgeons’ compensation varies with, or takes into account, the volume or value of their referrals; the court of appeals ruled that under the Stark Act, compensation “varies with” referrals if the two are correlated and compensation “takes into account” referrals if there is a causal relationship between the two. The court concluded that the structure of the surgeons’ contracts was enough to plead correlation and that the surgeons’ “suspiciously high compensation suggests causation” as well.
3. the hospitals either knew, deliberately ignored or recklessly disregarded that the surgeons received aggregate compensation that varied with or took into account the volume or value of referrals since UPMC controlled all of the hospitals and the subsidiaries that employed the neurosurgeons such that UPMC “has unfettered authority with respect to most members of the [medical system] and significant authority (including with respect to financial and tax matters) with respect to the remaining matters.” The court commented that many officers and board members of the various UPMC entities overlapped, noting that “[a]uthority was so centralized that a single person signed a settlement agreement on behalf of all the defendants that were part of the medical system. And with common control comes common knowledge.” The court concluded that the “common knowledge included both the surgeons’ pay and their referrals” (referring to the fact that UPMC took part in forming, approving, and implementing the surgeons’ pay packages and that UPMC has a central coding and billing department that handled billing for the subsidiaries). Accordingly, the court stated, “we can plausibly infer that the Medical Center knew the surgeons’ compensation varied with or took into account their referrals. And as the Medical Center knew that, so did the hospitals.”

The court of appeals decision goes into much detail parsing out what it means to “vary with” and what it means to “take into account.” According to the decision, “takes into account” means “actual causation;” the physician’s compensation must be based on or designed to reflect the volume or value of his or her referrals. “Varies with” means correlation; if compensation tends to

rise and fall as the volume or value of referrals rises and falls, then they vary with each other. The court reasoned that while the neurosurgeons' pay was "facially based only on the services they personally performed," every time they "performed a surgery or other procedure at the UPMC Hospitals, [they] made a referral for the associated hospital claims," which, according to the court, could be worth many times more than the neurosurgeons' own services. Accordingly, the court held, the neurosurgeons' salaries "rose and fell with their referrals" and "their aggregate compensation varied with their referrals' volume and value." In addition, the court held that the neurosurgeons' "suspiciously high compensation" suggests causation as well, noting that "common sense says that marked overpayments are a red flag" and that "[e]xcessive compensation is thus a sign that a surgeon's pay in fact takes referrals into account." According to the decision, whistleblowers must plead facts that make either correlation or causation plausible in order to meet the definition of indirect compensation arrangement under the Stark Act. The court found that the whistleblowers had done both in this case, pleading more than enough facts to suggest an indirect compensation arrangement exists between the neurosurgeons and the UPMC hospitals. Under this decision's analysis, any compensation model for a surgeon based on personal production meets the correlation test and, thus, will result in the presence of indirect compensation under the Stark definition.

After the court found that the whistleblowers had successfully pleaded all three elements of a Stark Act violation, the court quickly ran through the elements of a False Claims Act violation, since the whistleblowers pled their Stark Act claims as violations of the False Claims Act. The court expressly rejected the defendants' argument that the False Claims Act's falsity and knowledge elements make the applicability of Stark exceptions a required part of stating a False Claims Act violation. The court held that "[t]he burden of pleading Stark Act exceptions stays with the defendant under the False Claims Act." In ruling that the whistleblowers' pleadings satisfied all the elements of the False Claims Act, the court noted that (1) the defendants had submitted claims to the Medicare program; (2) the claims were alleged to be false because they were submitted in violation of the Stark Act and; (3) the complaint alleged that due to the defendants' corporate structure, they "at least recklessly disregarded" the possibility that the claims submitted violated the Stark Act and were, therefore, false. Once the court found that the elements of a Stark Act violation and False Claims Act violation were adequately pled, the court held that was sufficient for the complaint to survive the motion to dismiss stage and go to discovery.

The court of appeals rejected the defendants' argument that the neurosurgeons earn high salaries as a result of bona fide bargaining with their employers, because (1) at the motion to dismiss stage, the court "cannot go beyond the well-pleaded facts in the complaint;" and (2) the Stark Act "recognizes that related parties often negotiate agreements 'to disguise the payment of non-fair-market-value compensation'" and that "bona fide bargaining leads to fair market value only when neither party 'is in a position to generate business for the other.'" Accordingly, because the neurosurgeons and UPMC can generate business for each other, the court of appeals concluded that it "cannot assume that any bargaining was bona fide or that the resulting pay was at fair market value."

The court's decision was not unanimous. The concurring justice disagreed that the term "varies with" means correlation and stated that he "cannot agree that correlation alone is enough to show that compensation 'varies with, or takes into account, the volume or value of referrals' as required by § 411.354(c)(2)(ii)" and stated that he "would hold that this language requires some showing of an actual causal relationship to establish an indirect compensation arrangement." The concurring opinion noted that the court's decision suggests "that any hospital that pays its affiliated physicians according to some metric of the work they personally perform at the hospital falls under suspicion of violating the Stark Act, and it can only restore its good name by pleading one of the statutory exceptions—presumably at the summary judgment stage at the earliest, i.e., after discovery has already taken place."

In remanding the case to the district court for discovery and dismissing the concurring judge's concerns that this decision will open the floodgates of Stark Act/False Claims Act litigation, the court referenced the DOJ's authority to dismiss qui tam cases over a whistleblower's objection and notes that the government has "plenty of room to make good on its stated intention to scrutinize and dismiss more qui tam actions than in the past," leaving "little reason to fear that a flood of frivolous cases will reach discovery."

## Conclusion

Employed physicians such as surgeons, whose services are provided primarily in a hospital setting, will always have compensation that rises and falls with their referrals to those hospitals if the compensation is based on their personal production. Thus, the compensation arrangement between a hospital affiliate and its employed surgeon based on the surgeon's personal productivity would likely create an indirect compensation relationship and merely pleading the existence of that compensation arrangement would be sufficient to survive a motion to dismiss. If that is the standard to be used in evaluating compliance with the Stark Act, this case, if left to stand and followed by other circuits, will leave many hospitals and health systems vulnerable to similar lawsuits since physician compensation arrangements involving productivity-based compensation are widely used and have traditionally been considered acceptable under the Stark Act.

While this case only concludes that the whistleblowers have stated the basic elements of a violation of the Stark Act and False Claims Act and that the case should be permitted to go forward to discovery, the ruling in this case could mean that health care providers will be subject to more qui tam cases alleging Stark Act violations in which they will have to endure the discovery phase (at great expense) and get to the summary judgment stage before they are permitted to assert as affirmative defenses that one or more exceptions apply. The DOJ has not historically sought dismissal of most declined qui tam cases, so it is unlikely that it will protect many hospitals from that result.

# Authors

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