

Developing an Effective Pay-for-Performance Program

Legal and Practical Considerations for Hospital-Physician Contracts



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In this era of health care reform and accountable care, many hospitals are seeking opportunities to align physician interests with hospital programmatic, quality of care, and patient satisfaction initiatives. A well-crafted pay-for-performance (P4P) program can provide a hospital with a powerful tool to help achieve this alignment. Simply speaking, a P4P program is an incentive-based payment model designed to align the goals of a physician and hospital in a way that improves health outcomes and/or reduces costs to patients.

All P4P programs are subject to a variety of legal requirements, whether they appear as gainsharing arrangements or in the context of employment agreements, professional service agreements, or co-management agreements. Developing metrics for these types of incentives can be particularly challenging from a legal and operational perspective. This article highlights key legal considerations hospitals must keep in mind when developing the appropriate metrics for effective P4P programs.

Complying with Legal Requirements

P4P programs implicate a host of laws, including the Stark Law, the Anti-kickback statute, the Civil Monetary Penalties (CMP) statute and, for tax-exempt hospitals, federal income tax requirements for continued tax exemption. The parties to a P4P arrangement must pay particular attention to assure compliance with these legal requirements.

The CMP law subjects a hospital to a penalty if it “knowingly makes a payment, directly or indirectly, to a physician as an inducement to reduce or limit services” to a Medicare or Medicaid beneficiary who is under the direct care of the physician. Any physician who accepts such a payment is also subject to a civil money penalty. Developing metrics that do not have the potential to reduce or limit care is crucial to ensure compliance of the CMP law.

The anti-kickback statutes and the Stark Law generally prohibit a hospital from paying a physician to refer patients to the hospital. The anti-kickback statute is an intent-based statute and would be violated if even one purpose of the arrangement is to induce such referrals. To avoid a violation of the anti-kickback statute, it is important to develop a program that is primarily intended to improve quality outcomes and is not just a means to increase physician compensation.

To comply with the Stark Law, a compensation relationship with a physician must meet the requirements of an exception. A compensation arrangement can be designed to fit within an exception for employment, a fair market value contract, or a personal services contract. To satisfy each of these applicable Stark Law exceptions, compensation to the physician must be consistent with fair market value and commercially reasonable, and it may not take into account the volume or value of referrals by the physicians.

Developing Appropriate Metrics While Maintaining Focus on the Legal Requirements

In developing P4P metrics, it is important to maintain focus on the legal requirements. Key considerations include:

- P4P incentive compensation may not vary in any manner based on the value or volume of referrals that may be generated by physician participants for the hospital.
- The total compensation a physician earns, including compensation under a P4P program must reflect fair market value. It is imperative to engage a valuation consultant to provide an opinion that the compensation model will result in reasonable and fair market value compensation to the physicians.
- It is necessary to closely scrutinize incentive compensation metrics to assure they could not be construed as an inducement to reduce or limit care. Specifically, incentives based on reduced readmission rates or length of stay could implicate the CMP statute.

Practical Considerations

1. Do **NOT** base any component of P4P compensation on the value or volume of any referrals between the parties.

Example: Assume the applicable standard of care for all patients having a particular condition requires that each patient receive a certain imaging study. A P4P quality incentive based on achieving compliance with this standard of care could be deemed to be compensation that varies based on the value or volume of referrals (i.e. the physician must order imaging studies to comply with the metric and to achieve the P4P incentive).

2. **DO** assure that total compensation to the physician, including P4P incentives, remains consistent with fair market value.

Illustration: A physician employment compensation plan includes fixed annual base salary of \$200,000, administrative compensation of \$50,000 and a P4P bonus potential of \$30,000. The total potential compensation of \$280,000 must be consistent with fair market value.

3. Do **NOT** base any component of P4P compensation on measures that could induce physicians to reduce or limit care to patients.

Example: Hospitals have a real interest in reducing hospital inpatient length of stay (LOS) and readmissions, events largely managed by physicians. P4P incentives based on achieving or reducing LOS or readmission rates could be deemed to violate the CMP statute prohibiting payments to patients as inducement to reduce or limit services to Medicaid or Medicare beneficiaries.

Alternative: Consider developing a P4P compensation metric that rewards clinical behavior which is likely to have a positive impact on LOS or readmission rates. For example, building an incentive based on physicians managing post-discharge medication compliance by patients may reduce readmission rates.

In spite of the legal and operational challenges, properly structured P4P programs can serve to align hospital and physician goals of improving efficiency and quality of care. Like any payment arrangement between a hospital and physicians who refer business to the hospital, however, payments purportedly intended to encourage quality improvements might be used by parties to induce reductions in care or to disguise kickbacks for referrals. For those reasons, it is important to work closely with experienced legal counsel to develop metrics that reduce the risk of fraud and abuse and address the CMP law, the anti-kickback statute, and the Stark Law.