A Review of the Stark Law and Anti-Kickback Statute as Applied to Real Estate Transactions

This roundtable discussion is brought to you by the Real Estate Affinity Group (REAG) of the Hospitals and Health Systems (HHS) Practice Group.

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I. Quick Primer on AKS and Stark

✓ Anti-Kickback Statute

✓ Stark Law
Anti-Kickback Statute

The AKS prohibits the payment or receipt (and even the offer or solicitation) of any remuneration, *directly or indirectly*, either:

- ✓ To induce, or in exchange for, a *referral* of a person for services; or
- ✓ To induce, or in exchange for, the *purchase* of an item or service.

For which payment may be made in whole or in part under a federal healthcare program.
Anti-Kickback Statute  *(continued)*

- Remuneration
  - Can be cash, discount off fair market value, or even an opportunity to invest.

- Intent – Remuneration intended to induce referral or purchase of services
  - One Purpose Test – if even one purpose of the remuneration intended to influence referral or purchase of services.
Anti-Kickback Statute (continued)

✔ Lease “Safe Harbor”
  • Protects lease arrangements between referral entities if certain elements satisfied.

✔ Elements include:
  • Written agreement;
  • signed by parties;
  • describing all the space to be leased;
  • term not less than one year;
  • aggregate rent is set in advance over term of the lease;
  • rent is fair market value;
  • commercially reasonable business purpose.
Anti-Kickback Statute (continued)

✓ Applies not only to hospitals, but to any person or entity in a position to influence referrals.

✓ Criminal statute – requires intent.
  
  • Harder for Feds to prove, so not used as often as Stark (often enforced against physician groups);
  
  • Penalties include monetary fines ($25K per infraction), loss of eligibility, and PRISON.
Stark Law

A physician who has a financial relationship with a healthcare entity may not make referrals to that entity for health services (including inpatient and outpatient hospital services) for which reimbursement is sought from Medicare/Medicaid, and the entity may not bill for the provision of such services, unless the financial relationship fits within a specified exception.

**Penalties include:**

- monetary fines ($15K per fraudulent claim, $10K/day for failure to report, and $100K for each noncompliant arrangement);
- reimbursement of $$ to Feds;
- loss of eligibility.

**NO CRIMINAL INTENT REQUIRED TO PROVE STARK VIOLATION!**

- this means that a violation is a violation, whether intentional or inadvertent.
- no materiality threshold (even very minor violations are subject to severe penalties).
Lease Exception to Stark... leases must comply with all the following requirements:

- Written agreement, signed by the parties, which specifies the premises it covers;
- Term of at least one year;
- Space is reasonable and necessary for the legitimate business purpose and may include proportional allocation of common area expenses;
- Rent is set in advance and consistent with FMV;
Stark Law (continued)

- Rent not determined in a manner that takes into account the volume or value of referrals;
- Agreement commercially reasonable even if no referrals;
- Holdover month to month rental for up to six months immediately following an agreement of at least one year that otherwise met all the conditions above, provided the “holdover rental is on the same terms and conditions as the immediately proceeding agreement.”
Exposure to “Whistleblower” (*qui tam*) lawsuits…

✓ Stark violations are also considered false claims under the False Claims Act.

✓ False Claims Act allows private individuals to bring civil lawsuits alleging filing of false claims (disgruntled former employees, angry doctors, etc.)

✓ False Claims Act monetary penalties: up to $11,000 per claim X 3 (”treble damages”).

✓ Whistleblower financially incentivized, receives up to 1/3 of total amount recovered by Feds.
What is Fair Market Value?

How Fair Market Value is defined:

- **Fair Market Value** is defined as the value in arm’s-length transactions consistent with general market value.

- **Fair Market Value with respect to Leases** means the value of rental property for general commercial purposes, but can take into account additional costs incurred by the lessor in developing or upgrading the property.
What is Fair Market Value (continued)

- How does a Hospital landlord determine Fair Market Value?
- Hospital should obtain an appraisal (although not required by Stark).
- Appraiser should “opine” as to Stark definition of Fair Market Value.
- How often should you obtain an appraisal?
Healthcare Reform: Notable Changes in Compliance

New Rules of the Game:

✓ Fraud Enforcement and Recovery Act (FERA).
✓ Patient Protection and Affordable Care Act (PPACA).
✓ Health Care Education and Reconciliation Act.
Healthcare Reform: Notable Changes in Compliance (continued)

✓ FERA expands scope of False Claims Act (basis of most “whistleblower” lawsuits), imposes clear obligation on hospitals to make repayments of Medicare/Medicaid reimbursements that are disqualified due to Stark violation.

✓ PPACA requires hospitals to self-report (to CMS) violations, make repayments of disqualified claims.

  • PPACA also give CMS authority to negotiate and settle self-disclosed Stark violations w/o having to apply strict statutory penalties.

- Intent: to encourage self-reporting by holding out hope of favorable settlements.
- BUT, certain aspects of the disclosure protocols are potentially more onerous...
  - CMS can report voluntarily disclosed info to DoJ, OIG for further civil, criminal prosecution, including False Claims Act suits.
  - Parties must agree not to appeal any penalties assessed as part of any settlement.
- “Chilling Effect” on self-disclosure? Too early to tell, until more cases are settled under the new protocols.
  - No one wants to be the guinea pig.
  - End result may not be what the Feds intended.
Healthcare Reform: Notable Changes in Compliance (continued)

✓ Increased funding for Fraud and Abuse enforcement, projected expenditures of $350MM through 2020; Feds see high return on this investment, “low hanging fruit” to offset high cost of new government health care programs.
## Real Life Examples

<table>
<thead>
<tr>
<th>Organization</th>
<th>Fine</th>
<th>Reason</th>
</tr>
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<tbody>
<tr>
<td>Detroit Medical Center</td>
<td>$30 million settlement</td>
<td>Leases below FMV/no written lease</td>
</tr>
<tr>
<td>Condell Medical Center</td>
<td>$36 million settlement</td>
<td>Leases below FMV</td>
</tr>
<tr>
<td>Christus Spohn Hospital</td>
<td>$4.1 million settlement</td>
<td>Leases below FMV</td>
</tr>
<tr>
<td>St. James Healthcare-Montana</td>
<td>$275,000 settlement</td>
<td>No written lease</td>
</tr>
<tr>
<td>Ivinson Hospital-Wyoming</td>
<td>$635,000 settlement</td>
<td>Leases below FMV</td>
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Source: U.S. Dept. of Justice
Lease Scenario #1

- Hospital and Doctor sign a lease for a 5-year term on January 1, 2009.
- The lease provides that Doctor will pay his proportionate share of all operating expenses relating to the MOB (triple net lease).
- In January 2012, Hospital conducts a lease audit and realizes that Doctor has been undercharged for operating expenses during the term of his lease. Hospital has charged Doctor his proportionate share of operating expenses over a 2009 Base Year.
- Doctor’s lease did not include an operating expense Base Year or Expense Stop.
Lease Scenario #1 (continued)

✓ Hospital’s failure to correctly charge operating expenses was caused by a clerical error when the lease was entered into Hospital’s database.

✓ Has Hospital violated the Stark Laws and/or the Anti-Kickback Statute by failing to correctly charge operating expenses to Doctor?

✓ The uncharged operating expenses total approximately $30,000. Is Doctor liable for these uncharged operating expenses? Does the lease language require the Doctor to pay these operating expenses from 2009?

✓ Can Hospital and Doctor agree to settle these unpaid operating expenses with Doctor paying $15,000 of the $30,000 of uncharged expenses?
Lease Scenario #2

✓ Doctor leases 10,000 sq. ft. of space from Hospital for a 10-year term. Leased space contains $230,000 of tenant improvements (assume lease is fully signed and complies with all Stark Laws and the Anti-Kickback Statute).

✓ In addition to the 10,000 sq. ft. of leased space Doctor also uses an additional 100 sq. ft. of storage space in the MOB’s basement.
 Lease Scenario #2  (continued)

✓ Six months into the term of Doctor’s lease Hospital and Doctor realize that the parties never signed a lease for the additional storage space.

✓ Hospital typically signs leases with doctors in the MOB for these storage spaces.

✓ Does the parties failure to sign a lease for the storage space constitute a violation of the Stark Laws and/or the Anti-Kickback Statute?
 Lease Scenario #3

✓ Doctor has a “time-share” lease. The lease provides that the Doctor may use the leased premises from 8-12 on Tuesdays and Thursdays.

✓ Hospital discovers that the Doctor frequently uses the office on Thursday afternoons to complete “paperwork”, although the Doctor doesn’t see any patients. Does the Doctor’s use of the leased premises on Thursday afternoons constitute a Stark Law violation?

✓ Hospital also advises that the Doctor stores certain Medical equipment in a closet on a permanent basis. Does the Doctor’s use of this closet constitute a Stark Law violation?
Lease Scenario #4

✓ The Hospital built a 20,000 square foot MOB connected to the Hospital in 2008. The MOB has three tenants. Each of the tenants has a “triple net” lease. Each tenant moved in when the MOB was built in 2008.

✓ The Hospital discovers that the electrical service to the MOB’s lobby is included as a part of the Hospital’s electric bill. Are the tenants liable for their proportionate share of this unbilled electrical expense?

✓ Are the tenants liable for their proportionate share of other shared services (i.e. security, snow removal, etc.)?
Lease Scenario #5

✓ Doctor delivers a signed lease to Hospital’s leasing agent (Leasing Agent) on Thursday, June 26th for a lease that will commence on Tuesday, July 1st.

✓ Leasing Agent overnights the lease to Hospital’s corporate real estate department for signature.

✓ Doctor calls Leasing Agent on Friday, June 27th and advises Leasing Agent that he must move in over the weekend.

✓ Can Doctor move-in over the weekend prior to the commencement date of the lease? What if the Doctor doesn’t see any patients?
Lease Scenario #6

✓ Doctor and Hospital are negotiating a new 5-year lease for space in a MOB connected to the hospital.

✓ Hospital’s Broker advises that Hospital should charge $26 per rentable square foot for space in the MOB. Doctor believes that this rate is too high as Doctor can lease comparable commercial office space six blocks down the street for $20 per rentable sq. ft. Hospital would like to have Doctor “on-campus.”

✓ Hospital has obtained an appraisal of rental rates for commercial space within a half-mile of the MOB which states the fair market rental rate is $22-24 per rentable square foot for the market area.

✓ What rental rate should the Hospital charge to Doctor? If Hospital charged a rental rate of $26 per rentable square foot to Doctor, would such lease be Stark compliant?
Lease Scenario #7

✓ Doctor has been a tenant in Hospital’s MOB for 15 years.

✓ Doctor’s lease expires on March 31, 2012.

✓ Doctor advises Hospital that she will retire on June 30th. Doctor wants to remain in her suite until the end of June.

✓ Doctor’s lease provides that if Doctor holds over at the expiration of Doctor’s lease term, without Hospital’s consent, that Doctor shall be charged a holdover rental rate of 125% of Doctor’s then current rental rate.

✓ Can Doctor remain in her suite on hold-over status for three months?

✓ What rental rate should the Hospital charge to the Doctor during the holdover period?
Lease Scenario #8

✓ Doctor and Hospital sign a 5-year lease on June 1, 2009 for 3,243 rentable sq. ft. of space. Doctor and Hospital both believe that 3,243 rentable square feet is the correct square footage for the space. The lease language allows either party to re-measure the leased space pursuant to BOMA standards during the lease term.

✓ Hospital re-measures the MOB and the leased space on January 1, 2012 and discovers that the lease space was incorrectly measured at lease signing. The leased space actually contains 3,522 rentable sq. ft. of space according to BOMA standards.

✓ Should Hospital charge Doctor for this “extra” leased space? If Hospital charges Doctor for this “extra” leased space, should Hospital charge Doctor for this leased space as of June 1, 2009 or as of January 1, 2012?
Hospital Leasing Challenges

✓ Expired Leases.

✓ Failure to enforce Operating Expenses pass-throughs.

✓ Failure to implement annual rent increases required by lease terms.

✓ Providing tenant services not discussed in the lease (i.e., red bag service).

✓ Space occupied different from space described in Lease.

✓ Unsigned leases.

✓ Confirming FMV.

✓ Proper allocation of services shared with the Hospital.
Development Scenario # 1

**MOB Development – Without Master Lease**

**Goal:**
A hospital desires to have a new medical office building constructed on its campus.
Development Scenario # 1 (continued)

**MOB Development – Without Master Lease**

**Cast of Characters:**

- ✓ An acute care hospital (Hospital).
- ✓ A third party developer (Developer) which is unrelated to Hospital and which has no physician ownership.
- ✓ Physicians who are on Hospital's medical staff and who refer to Hospital (Physicians) and will occupy space in MOB.
Development Scenario # 1 (continued)

MOB Development – Without Master Lease

Facts of the Deal:

- Hospital ground leases unimproved land on its campus to Developer for 99 years.
- Ground lease to Developer contains a rental rate of $100.00 annually or some other nominal rate that is below fair market value.
Development Scenario # 1 (continued)

MOB Development – Without Master Lease

Facts of the Deal:

- Developer builds the MOB and directly leases suites in the MOB to Physicians.
- Hospital does not master lease any portion of the MOB.
- The rental rate charged by Developer to Physicians is consistent with fair market value rates, based upon appraisals of other medical office space in the community (assume $17.00 gross rent annually).
Development Scenario # 1 (continued)

**MOB Development – Without Master Lease**

**Facts of the Deal:**

- Developer is able to charge a $17.00 gross rate because Developer’s operating costs are less due to below fair market rent under the ground lease. Put another way, Developer would have charged higher rent to Physicians if Developer had paid higher ground lease rent.
Development Scenario # 1 (continued)

**MOB Development – Without Master Lease**

**QUESTION FROM THE HOSPITAL CLIENT:**

- Prior to executing the Ground Lease and other development documents, Hospital CEO wants you to bless the transaction from a Stark and
- Anti-kickback perspective.
Development Scenario # 1 (continued)

*MOB Development – Without Master Lease*

- **Hospital**
  - (ground lease - $100/ year)
- **Developer of MOB**
  - (FMV Leases)
  - Lease
    - Physician
    - Lease
    - Physician
    - Lease
    - Physician
Development Scenario # 2

MOB Development – With Master Lease

Goal:

A hospital desires to have a new medical office building constructed on its campus.
Development Scenario # 2 (continued)

MOB Development – With Master Lease

Cast of Characters:

- An acute care hospital (Hospital).
- A third party developer (Developer) which is unrelated to Hospital and which has no physician ownership.
- Physicians who are on Hospital's medical staff and who refer to Hospital (Physicians) and will occupy space in MOB.
Development Scenario # 2 (continued)

MOB Development – With Master Lease

Facts of the Deal:

✓ Hospital ground leases unimproved land on its campus to Developer for 99 years.

✓ Ground lease to Developer contains a fair market rental rate.
Development Scenario # 2 (continued)

MOB Development – With Master Lease

**Facts of the Deal:**

- Developer builds MOB.
- Hospital master leases the entire MOB from Developer for a rental rate of $20 per square foot annually. Master Lease term is 15 years with CPI annual increases.
- Hospital then subleases space to Physicians at a gross rental rate of $17.00 per square foot annually with CPI annual increases.
MOB Development – With Master Lease

Facts of the Deal

✓ Prior to executing the Physician subleases, Hospital obtains a “fair market rental study” from a licensed real estate appraiser which indicates fair market rental rates for similar buildings in the market are in the range of $16.00 to $18.00 per square foot annually.
MOB Development –
With Master Lease

QUESTION FROM THE HOSPITAL CLIENT:

✓ Prior to executing the Ground Lease and other development documents, Hospital CEO wants to know if you have any concerns regarding the transaction.
Development Scenario # 2 (continued)

MOB Development –
With Master Lease

Hospital

Developer of MOB

master lease $20 per square foot

(ground lease = FMV)

(sublease rental of $17.00 square foot = FMV)

Physician

Physician

Physician
Q&A

If you have a comment or question please press * 1 on your telephone keypad to enter the phone queue.
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