

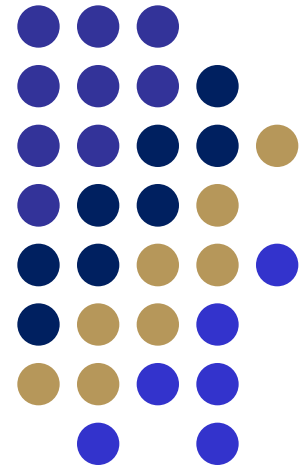
# Tuomey Case:

What the \$45 million Stark judgment teaches us about the uncertainties of FMV in physician employment deals

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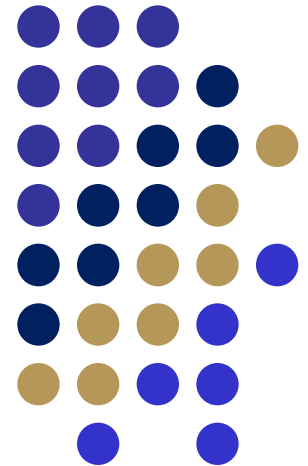
February 24, 2011



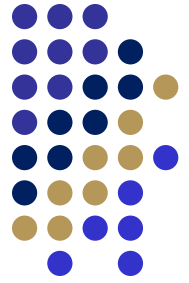
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**“Beware of little expenses...  
A small leak will sink a great ship.”**

*– Benjamin Franklin*



# Background



## Tuomey Healthcare System

- Anchored by Tuomey Regional Medical Center: 301 total beds
- 150 physicians on medical staff and 25 specialties represented
- Located in Sumter, South Carolina, a medically underserved and HPSA area, with a population of approximately 106,000 people living in the Sumter County Metropolitan Statistical Area
- Provides healthcare services to citizens in several surrounding counties

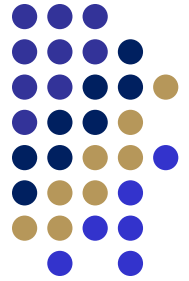


# What Led to This Case?



- Tuomey's response to competition from an ASC
- Need to retain specialists' outpatient procedures for continued financial performance
- Physician negotiations
- Dr. Drakeford, the Relator

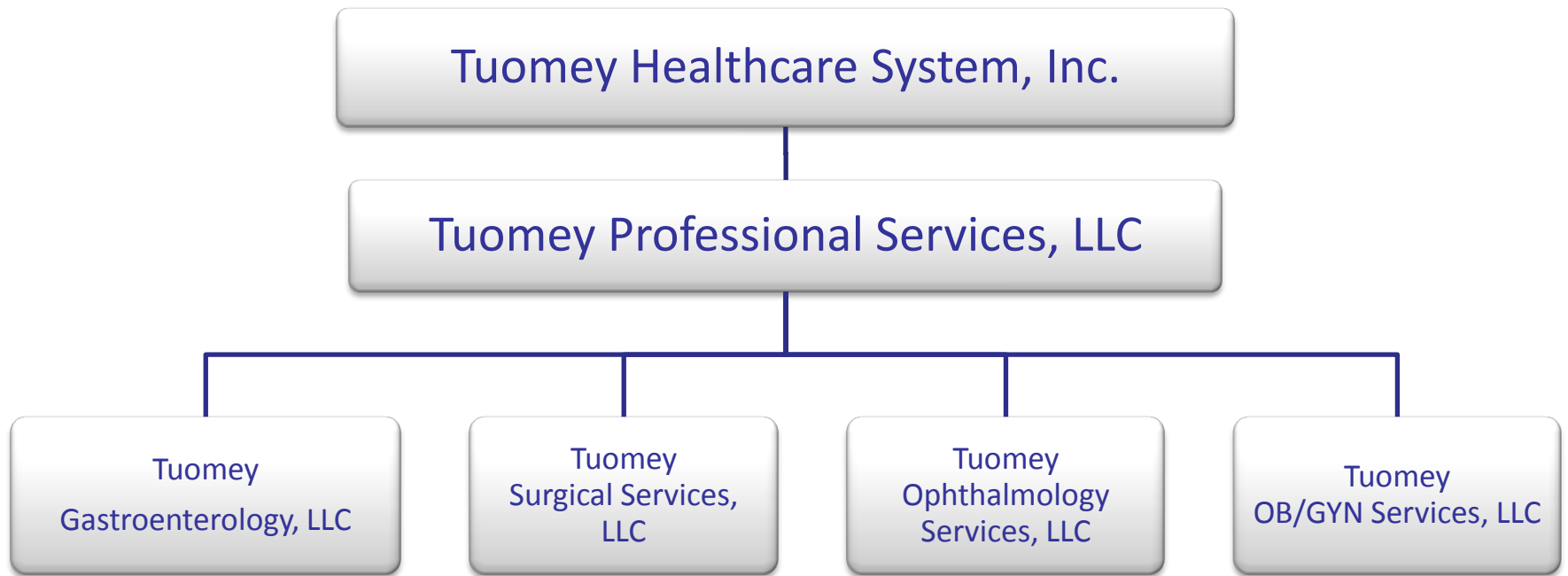
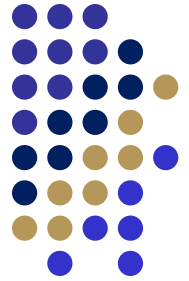
# Overview of FMV Components



**As evidenced in this case, even with an FMV assessment, many things can still go wrong:**

- Employment Contract; Terms and Commercial Reasonableness
- FMV Analysis
- FMV Pitfalls and Lessons Learned

# Employment Structure



# The Good, the Bad and the Ugly...

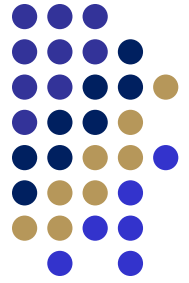
## You decide which is which



- Perhaps the first Stark/FCA allegation involving a battle of valuation experts
  - A valuation firm opined favorably on the subject transactions (at or near their inception).
  - An expert for the Government opined that the agreements were categorically above FMV.
  - An expert for the defendant opined that the subject agreements were categorically consistent with FMV.

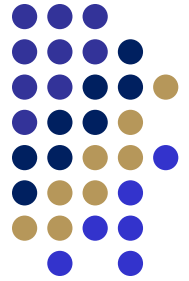


# The Valuation Opinion



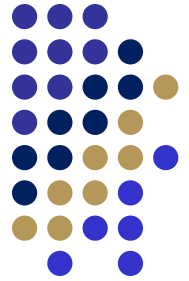
- Expert analyses are only as credible as the people who prepare them.
  - The consultants must be able to defend their conclusions.
  - The “user” of the report bears responsibility to ensure that the report appears credible.
- Cejka is now defunct as a valuation firm.

# The Government's Expert



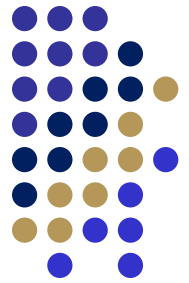
- Concluded that the physicians were paid in excess of FMV, the benefits exceeded FMV and the terms of the agreements were not commercially reasonable.
- Stated “Physician compensation at the median level is the accepted FMV level.”
  - *More on this point later...*

# Tuomey's Expert



- Concluded that the contracts were commercially reasonable and consistent with FMV.
- Embodied a more qualitative approach and analysis.
- Numerous individuals were interviewed.
- Cited difficulty in recruiting physicians.
- Cited opportunity to save the armed forces *millions of dollars...* (yet another qualitative aspect?)

# The Tuomey Employment Contract

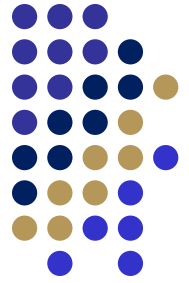


- Part-time employment covering only *outpatient procedures*
  - In some instances, only 5-10% of MD's overall activities
- Exclusive
- 10-year term (no cut), with a 3-year non-compete
- Base salary (based upon previous year's collections or procedures)
- Productivity Bonus (80% of collections)
- Incentive Bonus (up to 7% of Productivity Bonus)

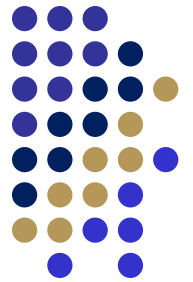


# The Tuomey Employment Contract

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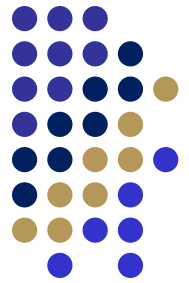
- Healthcare insurance
- Tuomey paid all malpractice premiums (including premiums covering the physicians for office services and inpatient procedures)
- CME reimbursement
- Cell phone reimbursement
- Periodical/Journal reimbursement



DAVE COVERLY

“WAS MY SALARY EXPECTATION A BIT TOO HIGH?”

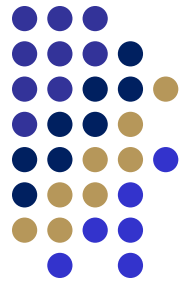
# Commercially Reasonable: To be or not to be...



## Government's position was:

- 10-year contract term is atypical.
- Part-time, partial services, contracts are unusual.  
(*i.e.* only outpatient)
- Compensation formula was flawed.
- Productivity bonus and incentive bonus kick in with first dollar earned.
  - % of collections arrangements not atypical...just usually better integrated.

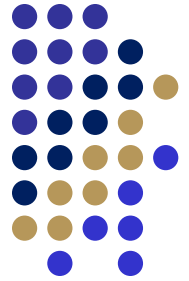
# Commercially Reasonable: To be or not to be...(cont.)



## Government's position (cont.):

- Doctors did nothing to earn base salary (*i.e.*, very few new administrative duties; no “identifiable services”).
- Full-time benefits to part-time employees was inconsistent with Tuomey’s normal policies (evidence of commercial unreasonableness perhaps).

# Commercially Reasonable: To be or not to be... (cont.)



## The Cejka Report

- In hindsight, the Cejka reports left much to be desired.
- The valuation reports are approximately 3 ½ pages in length.
- The valuation report was largely *qualitative* in nature.
- Cejka states “Higher total compensation is justified for higher levels of productivity.” However, the analysis indicates that the physician’s productivity fell between the 50<sup>th</sup> and 70<sup>th</sup> percentiles, yet compensation approximated the 80<sup>th</sup> percentile.

# Commercially Reasonable: To be or not to be... (cont.)

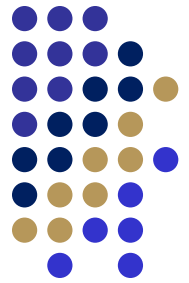


## The Cejka Report (cont.)

- A table within the report indicates that *net collections and total cash compensation* are nearly identical.
- No mention was made regarding “full-time” benefits for part-time employees.
- In its conclusion: “Cejka recognizes that this is an aggressive compensation plan that should be reviewed by a third party periodically to ensure that the terms continue to provide total compensation that is within fair market value.”
  - *Was this a litigation-ready document???*

# Employment Agreements

## FMV Analysis

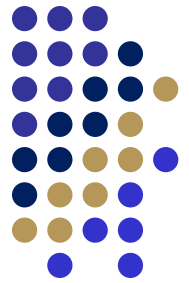


- Employment Agreements have many moving parts.... the “terms and features” are critically important.
- Available valuation methodologies
  - Cost
  - Income
  - Market
- The methodologies a valuator will deploy depend on the available data.
  - In an ideal situation, two or more methodologies would be applied.



# Employment Agreements

## FMV Analysis (cont.)



- ***Cost Approach***
  - Historical financials
  - Historical levels of physician productivity
  - Be aware of any key practice changes, cost reductions or reimbursement issues.
  - Past performance *may not* be a reliable indication of FMV.
- ***Income Approach***
  - Projected financials of the practice
  - Takes into account future changes in practice profile and reimbursement
  - Many people “overlook” the need to include a cost of capital/owner return line item in their projections.

# Employment Agreements

## FMV Analysis (cont.)

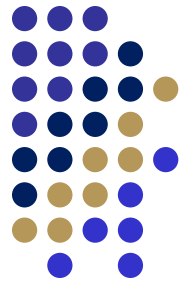


- ***Market Approach***

- Compares a practice/physician against available benchmark data
- Work Relative Value Units (“wRVUs”), professional collections, median compensation per wRVU; median compensation per professional collections
- Through linear interpolation of the data, match up each productivity variable with the expected level of compensation.

# Employment Agreements

## FMV Analysis (cont.)



### Compensation “Stacking”

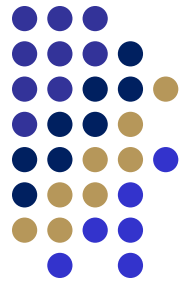
In all three approaches, if you label compensation layers by different names, you can stack them higher and higher!

- Sign-on bonus
- Productivity bonus
- Medical directorship
- Co-management agreement
- Quality bonus
- Retention bonus
- Call pay
- Tail insurance
- Excess vacation
- Relocation costs
- Excess benefits



# Employment Agreements

## FMV Analysis (cont.)

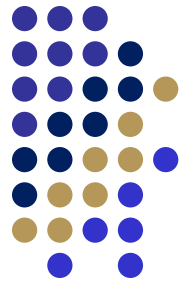


- In the case of Tuomey, the valuator chose to rely “solely” on the Market Approach...with perhaps misapplication of the market data.
- However:
  - Confucius Statistician say....If you torture the data long enough, it will confess to the crime it did not commit.
  - MGMA data can be misused in a variety of ways, including:
    - Cherry picking from among different tables (e.g., regional vs state data)
    - Failure to consider ownership/ancillary profits that may be inherent in 90<sup>th</sup> percentile compensation
  - Do regional compensation differences exist?  
The grass is always greener....



# Employment Agreements

## FMV Analysis (cont.)



### Example of misuse of MGMA data:

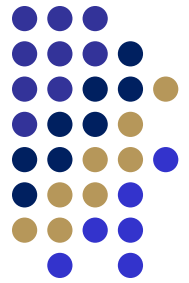
- Specialty in question: General Surgery
- 90<sup>th</sup> percentile cash compensation - \$550,000
- 90<sup>th</sup> percentile wRVUs – 10,798
- 90<sup>th</sup> percentile compensation per wRVU - \$76.02

### *Where is this going?*

- 90<sup>th</sup> percentile wRVUs x 90<sup>th</sup> percentile compensation per wRVU = \$821,000, representing 150% of 90<sup>th</sup> percentile
- MGMA states that there is an inverse relationship between physician compensation and compensation per wRVU.
- *Median* compensation (per wRVU) is a misnomer; no physician wants to be below the median!

# Employment Agreements

## FMV Analysis (cont.)

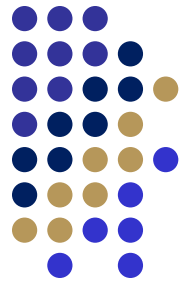


**In the context of these specific Tuomey arrangements, the Market Approach was used. However:**

- Physician's historical collections and procedure volume “benchmarked” at 25<sup>th</sup> and median (*i.e.*, 50<sup>th</sup>) levels, respectively.
- Benchmark data is reported on a F/T basis. When applying to P/T positions, this becomes an imprecise exercise.
  - Apportioned by hours worked?; productivity?
- Total compensation was calculated at approximately the 77<sup>th</sup> percentile.
- No specific mention of the “duties” (clerical or admin) provided in exchange for base compensation.
- Productivity bonuses “kicked-in” with first dollar earned.

# Employment Agreements

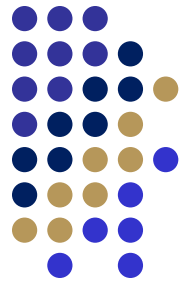
## FMV Analysis (cont.)



- Compensation formula categorically *guaranteed* it impossible to make money or break even on the practice.
  - May be permissible for certain specialties or in a “ramp-up” situation
  - Significant “stacking” issues were present as full-time benefits were provided to part-time employees.
  - Full malpractice premiums were paid even though only doing part-time outpatient work.
  - No sensitivity analyses were performed.
    - A model may make sense at certain productivity levels but not at others.

# FMV Pitfalls and Lessons Learned

....As inspired by the Tuomey Case



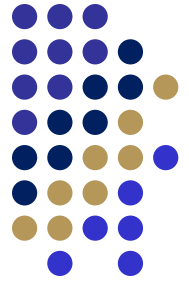
As stated at the beginning, even with a FMV assessment, many things can still go wrong.

- The terms and provisions assumed by (or told to) the appraiser may not match the Agreement.
  - 90% of “collections” versus 90% of “net income”
  - wRVU’s versus Total RVUs
- Did the FMV opinion consider multiple scenarios of the proposed compensation formula?
  - \$40/wRVU may work for low producers but could go awry at high levels of productivity.



# FMV Pitfalls and Lessons Learned

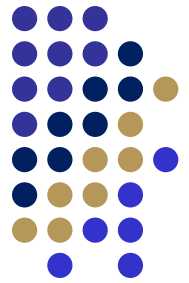
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- Difficult to support an employment arrangement with a largely “qualitative” opinion.
- Compensation arrangements can be very complex. Be cautious if an arrangement can’t be explained in a few sentences.

# FMV Pitfalls and Lessons Learned

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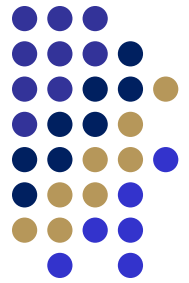


- Few, if any, standards exist for compensation valuation engagements or valuation firms. Independent valuation firms can each analyze the same data, and arrive at opposing conclusions (as in the present case).
- FMV reports should be read and critiqued (but by who?). Be sure to bring your magnifying glass. (See next slide.)
- Even for the reasonably well educated reader, it can be difficult to follow valuator's data, logic and conclusions. In light of the brevity of the Cejka report, it is fairly easy to read and react to. The litigation experts' reports (and many other FMV reports) require significantly more time and attention.



# FMV Pitfalls and Lessons Learned

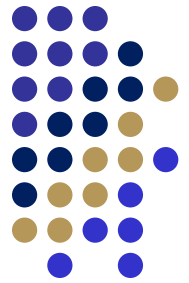
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- The sophistication of valuation approaches and reports has stepped up significantly over time.
- There are valuers of various capabilities, and certain firms may come and go. All the more reason to ensure that the report in hand appears defensible.
- Only recently has it come to general light that *median compensation per wRVU* provides “one” reasonable indication of FMV at many productivity levels.
  - Previously, it might have been logical to assume that a physician producing at the 90th percentile of wRVUs could be paid at the 90th percentile *compensation per wRVU*.
  - ***However, recall the prior slide and the lopsided compensation result!***

# FMV Pitfalls and Lessons Learned

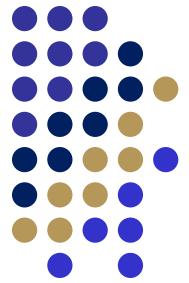
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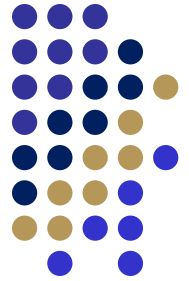
- With a Market Approach, it is beneficial to look at multiple sources of comparisons.
  - wRVUs, professional collections, median compensation to professional collections, etc.
- Make a “weighting” determination based on the unique facts of the particular arrangement and credibility of data.
- Depending on the specialty and/or sources of physician data, it may be that one “outcome” is more appropriate than another.

# FMV Pitfalls and Lessons Learned

(cont.)



- While “stacking” is a common sense concern, much more attention has been placed on this risk recently.
- The use of multiple compensation surveys (for multiple years) is advisable. However, dealing with discrepancies among the surveys can present a challenge. Physician compensation surveys are highly useful, but they contain anomalies.
- The use of “national” vs. “regional” data in the salary surveys continues to be a challenge. While regional data may seem more relevant, it can suffer significantly by virtue of smaller sample sizes.



"WE'D LIKE TO PAY YOU WHAT YOU'RE WORTH, TOO,  
DR. FENSTROM. UNFORTUNATELY, WE MUST  
COMFORM TO THE STARK LAW."

# Questions?

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**Thank you...**  
**Enjoy the rest of your lunch**

