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AMBULATORY SURGERY CENTERS BUSINESS AND LEGAL UPDATE

# Ownership and Referral Patterns

Physician investors often ask whether they can transfer interests amongst the investors or have an ASC or Hospital sell interests in order to create ownership of the Hospital or ASC that is in line with referral patterns to the Hospital or ASC. Specifically, this article discusses the issues of such transfers with respect solely to potential governmental claims and investigations in connection with the anti-kickback provisions of the Medicare/Medicaid fraud and abuse laws, 42 U.S.C. §1320a-7b(b) (the "Anti-Kickback Statute"). This article focuses solely upon the federal Anti-Kickback Statute.

The Anti-Kickback Statute prohibits the knowing and willful solicitation, receipt, offer or payment of "any remuneration (including any kickback, bribe or rebate) directly or indirectly, overtly or covertly, in cash or in kind" in return for or to induce the referral, arrangement or recommendation of Medicare or Medicaid business. 42 U.S.C. § 1320a-7b(b). A transfer of ownership interests in a surgical hospital or surgery center to existing or new physician investors in order to align interests in a manner that is closer to the volume or value of referrals made to the entity is likely illegal under the Anti-Kickback Statute. In addition, it can potentially raise issues under state self referral laws and a variety of other laws. The Anti-Kickback Statute prohibits any form of remuneration as a means to reward or induce referrals. Here, the proposed transfer could be perceived by the Office of Inspector General of the Department of Health and Human Services (the "OIG") as being provided in exchange for referrals to the ASC or hospital.

Violation of the Anti-Kickback Statute is a felony and may result in a fine of up to Twenty-Five Thousand Dollars ($25,000), imprisonment for up to five (5) years or both. In addition, the Office of Inspector General within the Department of Health and Human Services ("OIG") may suspend or exclude providers or suppliers from participation in the Medicare or Medicaid programs if it determines, in its discretion, that a provider or supplier has violated the Anti-Kickback Statute. 42 U.S.C. § 1320a-7b(b)(7).

The OIG has promulgated various safe harbors to the Anti-Kickback Statute that provide protection for certain financial arrangements. Safe harbors exist for a number of relationships, including investment interests in surgery centers and other small investment interests. Where a special opportunity is made for certain investors to buy shares, a transaction would not be specifically protected by a safe harbor. The OIG may scrutinize whether "any return on investment to the Physician-Investors [in a joint venture] will be proportional to their capital investments, and not based on referrals." Advisory Opinion 98-12 (September 16, 1998). Thus, it is important to be able to defend against allegations that any transfer or sale is being made to induce, reward or retain referrals from physician owners to the Hospital or ASC.

The pivotal issue under the Anti-Kickback Statute is intent. Direct evidence of intent to induce referrals, however, is usually lacking and, therefore, all relevant facts and circumstances bearing on intent must be examined to determine whether the intent necessary for an Anti-Kickback Statute violation exists. To prove a violation, the government must show both (1) an intent to induce or retain referrals, and (2) remuneration (offered or provid-

continued on page 2

# Twenty-Four Companies to Watch—2005 and 2006*

The following is a short note on twenty-four companies that are extensively focused on ambulatory surgery centers. Each has strong management and a growth orientation. We have highlighted these companies as those ambulatory surgery center companies to watch in 2005 and 2006. The list is in alphabetical order.

**1. Ambulatory Surgical Centers of America, LLC ("ASCOA").** ASCOA now owns and operates nearly 25 ASCs and some surgical hospitals throughout the United States. ASCOA has an extremely gifted and top flight management team. It executes plans very well. Unlike many operators, ASCOA prefers that physicians own the majority of the interests in the surgery centers that it operates.

**2. AmSurg, Inc.** AmSurg remains a leader in the operation and management of single specialty centers. It has a deep roster of centers (nearly 100) and it has highly principled and disciplined leadership.

**3. Ascent Partners.** Ascent provides management and consulting services to several ASCs. Tom Hui, a brilliant thinker, is the CEO of Ascent. It will be exciting to watch Ascent as they develop and implement their plans.

continued on page 3

## INSIDE

**Ownership and Referral Patterns** **continued from page 1**

ed) in exchange in any form whatsoever for such referrals. Case law interpreting the Anti-Kickback Statute has generally interpreted the restriction broadly in that remuneration is illegal if any portion of the remuneration is intended to induce referrals and remuneration can include "anything of value in any form whatsoever." See U.S. v. Greber, 720 F.2d 60 (3rd Cir. 1985), and, U.S. v. Kats, 871 F.2d 105 (9th Cir. 1998).



Because physician-hospital relationships are receiving increased scrutiny from the OIG and generally under the Medicare/Medicaid program, it is extremely important that parties be able to clearly document the intent behind any transfer of shares (i.e., that the actual intent is not intended to induce or reward or retain referrals in any manner). For example, is the transfer made to equalize all holders of shares or is it made solely to raise capital and do all holders have the right to buy shares.

The OIG has characterized an offering of shares in a joint venture as suspect when it:

> may be intended not so much to raise investment capital legitimately to start a business, but to lock up a stream of referrals from the physician investors and to compensate them indirectly for these referrals. Because physician investors can benefit financially from their referrals, unnecessary procedures and tests may be ordered or performed, resulting in unnecessary program expenditures.

59 Fed. Reg. 65373-74 (Dec. 19, 1994). Here, if there is any sense that shares are being offered only to investors who are bringing substantial volume and not to all investors and the effect is not intended to equalize holdings, it may be difficult to defend the transfer of shares as not being made to reward, retain or induce referrals to the Hospital or ASC.

In summary, a transfer or sale of interests solely to higher volume producers possesses substantial risk under the Anti-Kickback Statute. ■

**Twenty-four Companies to Watch—2005 and 2006** continued from page 1

**4. Aspen HealthCare, Inc.** Aspen manages hospital physician joint ventures and physician-owned ASCs. Aspen traditionally has not had an ownership interest in the ventures it manages. Aspen now also invests in ASCs. Tom Yerden, the Aspen CEO, and Aspen have continued as a nationally renowned leader in the ASC business and currently works with close to 30 surgery centers.

**5. Cirrus Health.** Cirrus, based in Texas, has developed centers and surgical hospitals in California and Texas and is expanding rapidly. It appears to have done a tremendous job of developing market research specific to each location. It has a tremendous recipe for success and terrific plans for future success and growth.

**6. HCA The Health Care Company, Inc.** HCA has over 265 facilities (approximately 190 hospitals and nearly 80 ASCs). HCA is currently the largest owner and operator of hospitals in the U.S. HCA has reorganized its outpatient division as one of three core divisions of the Company. It has made Marilyn Tavenner the head of the division and Greg Beasley the leader of the ASC team within that division.

**7. Health Inventures.** Health Inventures is one of the long-standing leaders in the ASC management and development business. It now also invests with its clients in projects. It does work across the United States and in England. It appears to be on a quick growth pace.

**8. Healthmark Partners/Surgical Health Partners.** Healthmark Partners currently operates nearly ten centers of which a handful have hospital partners. It also has several centers under development. It focuses on start up and turn around centers. The company has a reputation for being a pleasure to work with.

**9. Health South ("HS").** HS is a national operator and manager of surgical centers. Currently, it is the operator of approximately 200 ambulatory surgery centers. HS appears to have cleaned up several issues with the DHHS and is again beginning to assert itself as a market player.

**10. Integrated Medical Delivery ("IMD").** IMD is one of the few companies which focuses on providing the back office services needed by ASCs and hospitals. IMD appears to do very good work and is very energetic. Its model can help hospitals reduce start-up costs. IMD allows its clients to select some or all of the services they desire to use. Its initial hospitals and centers have been quite successful. IMD believes in 100% physician ownership of the hospitals and surgery centers it works with.

**11. Medical Facilities Corporation ("MFC").** Newly public, MFC is led by Dr. Larry Teuber. The company owns several

continued on page 4

**Twenty-four Companies to Watch—2005 and 2006**
**continued from page 3**

surgical hospitals. It is aggressively seeking acquisitions. Dr. Teuber is a brilliant strategist.

**12. National Surgical Care ("NSC").** NSC has really started to hit its stride. NSC has completed several acquisitions. It appears poised for a doubling of its size in the near future. Its management team is of very high quality.

**13. National Surgical Hospitals ("NSH").** NSH is the leader in owning and operating surgical hospitals. It has a top flight management team.

**14. NeuroSource, Inc.** NeuroSource is a leading neurosciences company. It specializes in efforts related to the neurosciences. It owns a hospital in Chicago and has helped other hospitals to develop their neurosurgical programs. It also operates and leases gamma knives and other high tech equipment.

**15. Nueterra Healthcare.** Nueterra is an owner and operator of dozens of centers and some surgical hospitals. It has made substantial efforts to enhance its operations over the last couple of years and seems to be benefiting greatly from such efforts.

**16. NovaMed.** NovaMed is one of the few companies that has successfully made the transition from practice management

**continued on page 11**

# The Anatomy of a "Do Over"

**Robert Zasa, Principle-Woodrum/ ASD, 6264039555**

There is a movie with the name City Slickers that was popular in the 1980's. Three men are on a dude ranch, cattle drive trying to find themselves and reorient their lives. One in particular has had an affair and his father-in-laws business and has a result has gotten divorced, lost his job, and his children. His best friend tells him his life is a "do over", just like when they were kids playing stick ball and a mistake was made. Everybody understood that it wasn't the right thing to do immediately and they would ask each of their friends to "do over" the play. Managing an organization is similar. Management is a series of plays that are called and the team has to execute them. Sometimes mistakes of commission or omission occur. Sometimes, the players don't get along. Sometimes, the play book becomes stale or predictable. And what about the new players? How are they brought along to participate and still understand the team's goals? Sometimes a new coach or quarterback with new plays is necessary to get the team back on track. That's a "do over". There are a lot of ASCs that are five years and older since their inception. Many of them are do overs or at the very least need to be refreshed. One starts with the recognition by all of the parties in particular in the governing body, that new ideas are needed to be interjected. And outside objective parties should be retained to review the current situation and walk the governing board through the steps of reorganization. This should be done with the key owners and users. Legal review of all of the documents, evaluation by an experienced source, and an operational review of both the revenues and expenses should be completed.

Key elements to review in a "do over".

### The Organizational:

- The age and number of current physicians.
- How many new physicians want to buy in?
- The current price per share or unit of the ASC.
- The history of the dividends with the amount that has been paid.
- The frequency of the distributions.
- Competition in the area.
- The price per share or unit at that competitive ASC.
- Does the ASC entity have both the ownership of the business and the land the building is in it or just the business of the ASC.
- Who owns the land and building and equipment.

### Legal Considerations:

- When was the last time that the legal documents were reviewed and/or redone?

continued on page 6

**The Anatomy of a "Do Over" continued from page 5**

- What is the status of the bylaws?
- What is the status of partnership agreement?
- How are the documents handled buying out partners or members?
- How are the documents handled retired or relocated physicians who are not currently active in the center or otherwise non-productives?
- What is the buy-in method and formula?
- What is the buy-out method and formula?
- Do the documents reflect the current healthcare regulations and laws both federal and state?

### Revenue Issues:

- Pricing strategy.
- Retroactive payer contract review of current plans.
- Which plans to keep and should the center apply for out of network benefits.
- Collection results and policies.

### Operational Costs:

- Cost of medical supplies and drugs.
- Current inventory and ability to reduce it creating a more distributable cash.
- GPO arrangements including pricing level.

### Staffing:

- What is the pay scale?
- Length of employment by employees?
- The payroll.
- What are the costs of the benefit plan?
- Illness.
- Contract labor and overtime.

### Service Contracts:

- How many service contracts are there?
- What are the costs of the service contracts?
- Are the service contracts related to the building incorporated in the rent or are they separate?

### Professional Fees and Contracts:

- Medical Directors contract.
- Legal retainer and fees.
- Accounting contract and fees. What services are being requested on an annual basis?
- Management contract and fees. What services are to be deliverable for a year?
- For all of the contracts, what is the value for what is being paid?

### Equipment and Building Financing:

- What are the existing amounts and terms of debt for the equipment financing?
- What are the existing amounts in terms of debt for the building financing.
- What is the length of debt for each of these?
- Can these expenses be improved upon by refinancing?

### Accounts Receivable:

- Review the balance sheet and assure that the balance sheet reflects the truly collectable accounts receivable.
- What happens to accounts greater than 90 days? How many are there and what is the collection experience on these accounts?
- Can these accounts be collected (that review the age and quality of the accounts) to maximize the realized revenues.

### Building Lease:

- Review the current lease rate and terms.
- What increases are expected over the next several years?
- Is the lease triple net (does not include maintenance, taxes, and utilities) or is it a gross lease or a modified gross lease?
- Who owns the real estate?
- Is the lease an arms length arrangement between members that also own the surgery center or is there a third party involved?
- What should the lease look like in that market to be at a fair market value?

Once a review of all of these data occur, key decisions need to be made and they are as follows:

### Key decisions to be made:

- Who will remain as owners?
- How will the previous owners of the ASC or now inactive be brought out?
- What new partners, if any, will be brought in to replenish the pool of participants in the ASC?
- What will the financial projections of the newly reorganized ASC look like?
- What was the valuation of the old ASC?
- What improvements in the legal documents should be made?
- What are the total costs of the "do over" and the economic benefit from doing it?

These steps "do over" can get you back in the game. ■

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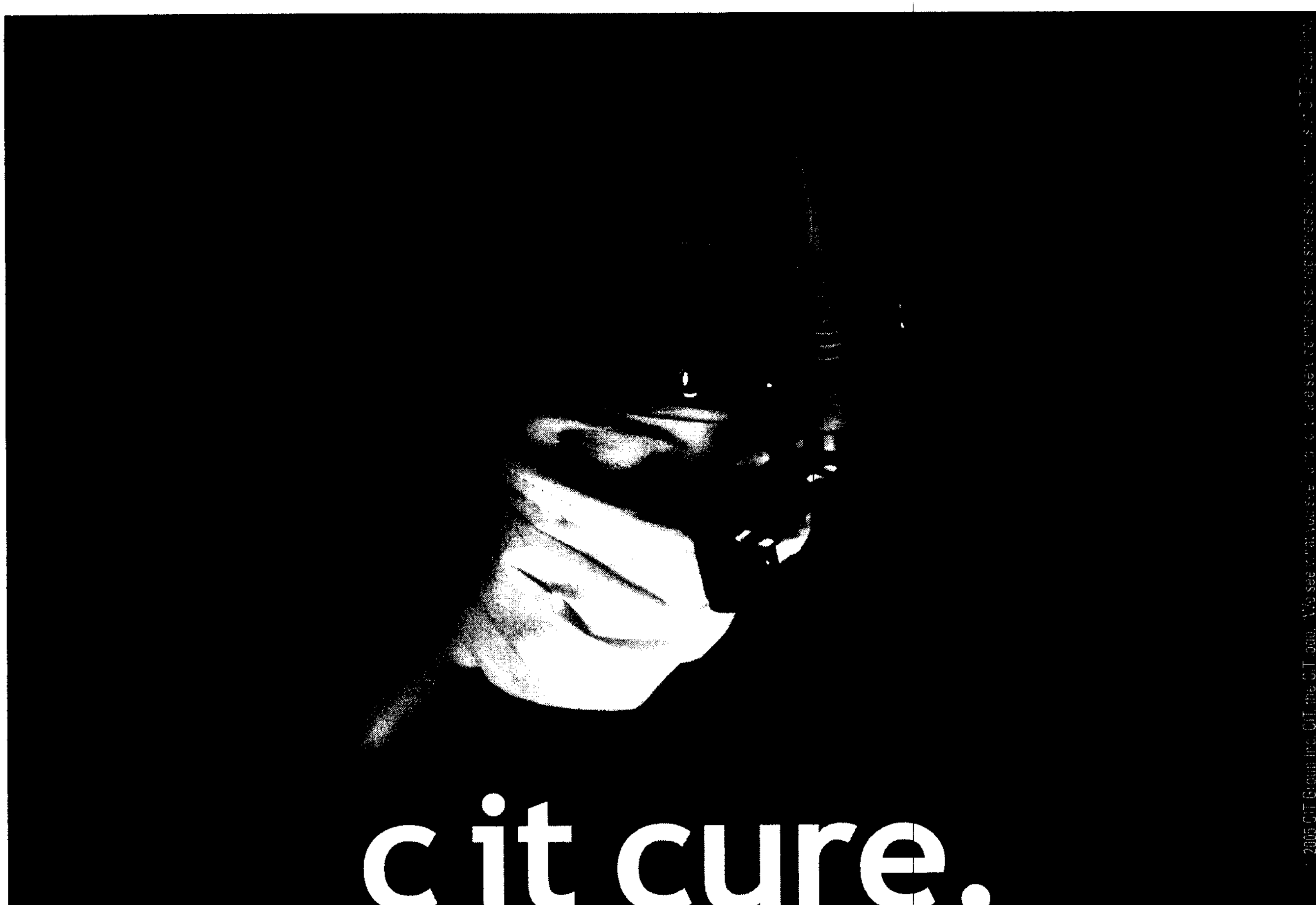

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Twenty-four Companies to Watch—2005 and 2006 continued from page 4

to facility ownership and operation. It has a close-knit and dynamic leadership team. We commend their efforts.

**17. Physicians Endoscopy, LLC ("PE").** PE owns minority interests in and manages nearly a dozen endoscopy centers. It recently opened centers in several new states. It has an extremely diligent and high integrity management team. PE remains a leading company in the management of single specialty endoscopy facilities.

**18. Regent Surgical Health, LLC.** Regent, based in Chicago, Illinois, develops, turns around and manages surgical centers. It has become a very strong participant in the surgery center industry, with centers in California, Arizona, Nevada, Ohio and Indiana. It provides management services and owns minority interests in surgical centers and hospitals. Regent has specialized in helping to stabilize and turn around surgery centers.

**19. Surgery Center Solutions.** This company, founded by a high integrity ASC veteran, helps hospitals to develop joint ventures with their physicians. Surgery Center Solutions has completed a few joint ventures and is on the road to complete several other ventures in the coming year.

**20. Surgery Consultants of America.** This company, founded by Caryl Serbin, provides management and development and billing services to surgery centers. Its efforts are focused on both physician only ventures and physician hospital ventures. Surgery Consultants takes a very hands-on approach to its efforts and has provided great assistance to numerous ventures. It is a very service-oriented company. It provides exceptional services.



**21. Surgis.** Surgis was developed by a former leader in the practice management business. It has an experienced management team and has raised substantial capital to fund its operations and growth. It has fueled its recent growth through the acquisition of individual centers as well as a company that owned a number of ASCs. It has really improved its efforts over the last two years and seems to be doing a great job.

**22. Symbion Inc.** This company, which went public nearly 18 months ago, is headed by a top management team. It has hit its stride and is doing a great job in developing and managing ambulatory surgical centers. Symbion typically owns a majority interest in centers. It is a leading buyer of ASCs and has a strong influence in the market place.

**23. United Surgical Partners International, Inc. ("USPI").** USPI is a national leader in the operation of multi-specialty physician hospital surgery centers. USPI currently has centers and hospitals throughout the United States. The company is doing a great job and is the best of class in the hospital-management company-physician joint venture ownership model.

**24. Woodrum/ASD and its affiliate ReSurge Hospitals.** Woodrum/ASD, founded by Robert Zasa, Joe Zasa and David Woodrum, manages and assists in the development of a wide variety of outpatient services for hospital and physician clients. Woodrum/ASD's principal focus is on ambulatory surgery centers. Its affiliate, ReSurge Hospitals, led by Rusty Shelton, has made great strides in the business of developing and managing surgical hospitals. The two companies currently have a wide variety of projects in diverse markets from Texas to Illinois to California to Alabama and several other states. It had an extremely busy and successful 2004. ■

*This list has been compiled by Scott Becker, Co-Chairman of the Health Care Department at McGuireWoods LLP. It is not intended to reflect an endorsement of any such company. Should you have questions regarding any of the companies listed herein, please contact Scott Becker at (312) 750-6016.