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A Call for Increased Oversight of Physician Compensation

Presented by Integrated Healthcare Strategies
as Authored by Mark Ryberg

In recent years, we have seen a dramatic increase in regulatory scrutiny in the not-for-profit health care sector. By and large, the aim of this scrutiny has been focused on what is perceived as fraud in the health care marketplace, ultimately resulting in overpayment by the federal government. In addition to the interest in Medicare and Medicaid fraud, federal regulatory agencies are increasingly interested in the breadth of financial relationships that exist between health care organizations and physicians, in particular, compensation arrangements.

As a result of this growing interest, it is imperative that organizations establish processes for ensuring adequate oversight of physician financial arrangements. Today, it is critical that health care organizations closely scrutinize their financial relationships with physicians for two principal reasons. First, these organizations need to ensure these relationships meet and/or exceed current regulatory requirements. Second, these relationships need to be commercially reasonable as they are fundamental to the long-term financial viability of these organizations.

Key definitions for organizations in the area of physician compensation include the following:

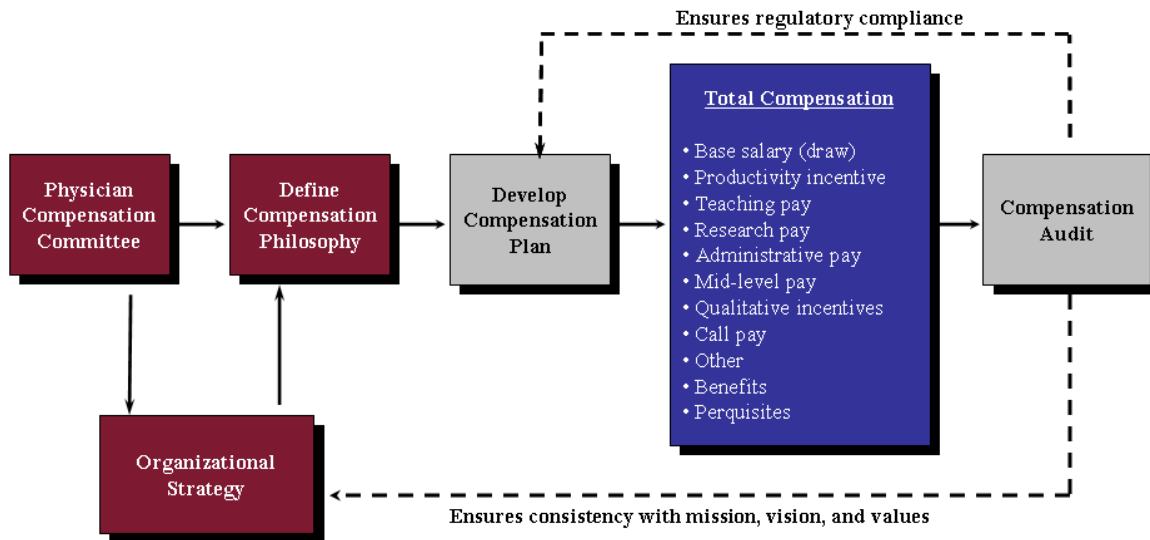
- **Fair Market Value (FMV)** - defined as the value in arms-length transactions consistent with the general market value. General market value means the price an asset would bring as a result of bona fide bargaining between well-informed buyers and sellers who are not otherwise in a position to generate business for the other party.
- **Commercial Reasonableness** - defined as an arrangement that would make commercial sense if entered into by a reasonable entity of similar type and size and a reasonable physician of similar scope and specialty, even if there were no potential designated health services referrals.
- **Reasonable Compensation** - as described in Section 162 of the Internal Revenue Service (IRS), reasonable compensation is generally considered to be "...only such amount as would ordinarily be paid for like services by like enterprises under like circumstances."

Best Practices

Many of the best practices for governing physician compensation are similar to those for governing executive compensation and benefits, such as:

- Establishing a board committee dedicated to physician compensation
- Developing a written charter that defines the committee's purpose, outlines its responsibilities, and establishes the process by which it will carry out those responsibilities
- Maintaining regular minutes and a calendar of scheduled meetings
- Developing a physician compensation philosophy that addresses the following:
 - Establishes the purpose of the compensation philosophy, including the importance of aligning physician incentives with the mission and values of the organization
 - Defines the guiding principles and objectives for the physician total compensation program, including a description of the values underpinning the program (e.g., competitiveness, equity, compliance, etc.) and a linkage to the organization's tax-exempt mission and role in the community
 - Establishes compensation parameters for employed and contracted physicians with respect to each of the categories of compensation (e.g., salary, productivity incentive compensation, quality incentive compensation, administrative compensation, benefits, etc.)
- Establishing an organizational policy that governs the administration of the compensation program:
 - Delegates day-to-day oversight of physician compensation to administration
 - Establishes a contracting and documentation protocol
 - Requires regular review of all aspects of compensation
 - Establishes a process whereby the organization utilizes quantitative data as well as an outside consultant(s), as necessary, to evaluate physician compensation
 - Establishes operational parameters that dictate when review/approval by the committee is required

The following illustration provides a simplified outline as to how these best practices apply for physician compensation governance:



Maintaining Good Governance

Once the key elements outlined in the previous section are in place, the administration and/or physician compensation committee has an oversight role to ensure that physician compensation is administered appropriately within the organization. In general, each financial relationship between a hospital and a physician must satisfy five elements of review and approval:

1. Health care objectives (i.e., mission) assessment
2. Fair market value review and documentation
3. Legal review
4. Review and approval by the compensation committee (if necessary)
5. Execution of a written agreement outlining the arrangement

In addition to developing a compensation program that is consistent with market practice and routinely auditing the program to ensure compensation levels are reasonable, it is imperative that organizations actively oversee physician compensation on an ongoing basis. To that end, our Physician Services practice advises our clients that thorough documentation is the cornerstone of a defensible physician compensation program. At the outset, an organization must document its strategic rationale for entering into a financial arrangement with a physician. During the course of that relationship, the organization must ensure that any and all compensation remains consistent with market and that the organization obtains the services for which it has paid (e.g., time reporting for non-clinical physician services such as medical directorships).

As oversight obligations become more onerous, many organizations on the forefront of best practice are developing a central database that houses all relevant information pertaining to each and every financial relationship between the organization and a physician. This information includes the strategic rationale(s) for the arrangements in question, current contracts as well as a mechanism to identify upcoming expirations, annual quality incentive metrics, performance reviews, job descriptions for both clinical and non-clinical functions, actual historical compensation paid by component and in total, time records for each administrative/non-clinical role for which the physician received compensation, a curriculum vitae, etc. Those organizations that actively monitor and thoroughly document any and all financial arrangements with physicians are best positioned relative to the next wave of regulatory scrutiny.

About Integrated Healthcare Strategies

Integrated Healthcare Strategies provides not-for-profit healthcare organizations with direct access to a comprehensive array of healthcare-specific services, delivered by professionals from the industry who understand the rigors of running a healthcare organization – from the lunchroom to the Board Room. Its client list is a “who’s who” of healthcare organizations including over 1200 major healthcare providers, 1,800 hospitals and 700 independent and affiliated medical groups. Integrated Healthcare Strategies specializes in the areas of physician strategy and compensation, employee compensation, executive compensation, human capital solutions, labor relations, leadership transition planning, executive search, employee surveys, performance management and board governance solutions.

About the Author

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The Physician Services practice of Integrated Healthcare Strategies helps create successful relationships between healthcare organizations and their employed and affiliated physicians by providing unique consulting services that focus on physician total compensation plan designs, fair market value and commercial reasonableness (including Professional Services Agreements), organizational structure and physician leadership development. For more information, visit www.IHStrategies.com, or call 800.327.9335.