LEGAL CORNER

Use Caution When Undertaking a Joint Venture

by Karen S. Lovitch, Esq., and Stephen R. Bentfield, Esq.

In the 1990s, the Office of Inspector General (OIG) adopted safe harbors that can protect the parties to a joint venture. With regard to physician-hospital joint ventures, the most significant of these safe harbors, which became effective in 1991, applies to small investments. Unfortunately, the requirements of this safe harbor are quite onerous, especially the "60/40 Rules." These rules dictate that investors in a position to generate business for the venture cannot have held more than 40 percent of the value of the investment interests of each investment interest class in the previous fiscal year or in the previous 12-month period. These rules also state that business generated by the investors cannot amount to more than 40 percent of the venture's gross revenue from healthcare services in the same time period.

In 1999 the OIG adopted a safe harbor for investment interests in healthcare entities located in medically underserved areas. This safe harbor's requirements are substantially similar to the small investment interests safe harbor, except that the 60/40 Rules are replaced with a 50/50 Rule. This safe harbor also dictates that 75 percent of the business in the previous fiscal year or in the previous 12-month period must come from services furnished to persons in a medically underserved area or to persons from a medically underserved population.

In 1999 the OIG also promulgated a safe harbor protecting ownership interests in ambulatory surgical centers (ASCs). This safe harbor is broken down into four categories, one of which is hospital/physician-owned ASCs. The most significant aspect of this safe harbor is the requirement that the hospital cannot be in a position to make referrals to the ASC, which, in many instances, effectively prevents compliance with this safe harbor.

In April 2003 the OIG published a Special Advisory Bulletin on contractual joint ventures. Here, the OIG questioned joint venture arrangements in which one party (e.g., a hospital) contributes only referrals to the joint venture while the other party (e.g., a durable medical equipment company) provides the inventory, employees, space, and essentially all other items and services necessary to operate the joint venture.

Since April 2003 the OIG has issued a handful of Advisory Opinions addressing the legality of various joint ventures. Although an Advisory Opinion is issued only to the requestor and therefore cannot be relied upon by any other individual or entity, such pronouncements can provide insight into the OIG's current position on various arrangements. In Advisory Opinion 03-12 (May 29, 2003) and Advisory Opinion 03-13 (June 23, 2003), the OIG gave some comfort to providers by finding that the joint ventures proposed therein posed minimal risk under the Anti-Kickback Statute even though neither fell squarely within the terms of any safe harbor. In contrast, the OIG viewed a proposed pathology services joint venture unfavorably in Advisory Opinion 04-17 (December 17, 2004) because the physician groups would be expanding into a related line of business that would be dependent upon referrals from the groups, and they would have no responsibility for the laboratory's operation. The OIG concluded that the proposed pathology joint venture exhibited the suspect characteristics identified by the OIG in its April 2003 bulletin.

To mitigate risk when forming a hospital-physician joint venture, consider the following safeguards, especially if the arrangement is not in strict compliance with a safe harbor:

- The venture should not have a captive referral base supplied by one or more participants.
- One investor should not bear disproportionate responsibility for the venture's operation or financing.
- Neither the terms on which an investment in the venture are offered nor returns on the investment should be based on the volume or value of referrals.
- The hospital should not require or encourage affiliated physicians to make referrals to the venture and should not premise compensation of physicians directly or indirectly on referrals to the venture.
- The venture should offer investment interests and also market or furnish items or services to passive and other investors on the same terms.
- Each investor's return on investments should be proportional to its capital investment.
- Participants should maintain appropriate documentation of the venture's goals, structure, and operation.

Given the financial and technological pressures on today's oncology providers, a joint venture with the right partner could make cost-effective treatment available to more patients. However, careful consideration must be given to choosing the correct structure and partner, and sound legal advice on this constantly evolving area of the law should be sought every step along the way.

Karen S. Lovitch, Esq., and Stephen R. Bentfield, Esq., are with the Washington, D.C., law firm of Mintz, Levin, Cohn, Ferris, Glovsky & Popeo, P.C.