



## ALABAMA STATE BOARD OF MEDICAL EXAMINERS

LARRY D. DIXON, EXECUTIVE DIRECTOR

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April 17, 2007

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Richard L. Sharff, Jr.  
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### DECLARATORY RULING

Dear Mr. Sharff:

This ruling is issued pursuant to your written request for a declaratory ruling from the Alabama State Board of Medical Examiners concerning the application of Alabama Code §34-24-360(10) to the factual situation stated in your January 22, 2007 correspondence. The Board understands that the following factual background constitutes the basis for your request:

#### **Factual Background**

An independent pathology practice (Laboratory) seeks to enter into a written services agreement with a professional association of urologists (Urology Group) for the provision of certain pathology services by the Laboratory to the Urology Group. Under the agreement, the Urology Group would bill third party payers and/or patients (when applicable) for all services and would retain all amounts collected with respect to such billings. As payment for services rendered, the Urology Group would pay the Laboratory a fee in an amount equal to a fixed percentage of the sum collected by the Urology Group. This fee would be negotiated between the parties and would be established in advance of the provision of any services. It would remain unchanged for the duration of the initial one year term of the agreement but would be subject to renegotiation only in connection with the annual renewal of the agreement. The fee would be set at a level constituting fair market value compensation to the Laboratory and would be based upon the anticipated volume of work by the Laboratory and the historical need of the Urology Group for anatomical pathology services. Under the terms of the agreement, the Urology Group would not be required to purchase any minimum volume of services from the Laboratory. Further, the proposed arrangement would be nonexclusive, allowing the Urology Group the option of obtaining pathology services from any person or entity of its choice. Likewise, the Laboratory would also have the option of offering its technical and professional services to any other person or entity of its choice.

### **Legal Analysis**

It should first be pointed that the current Opinions of the Council on Ethical and Judicial Affairs for the American Medical Association, which interpret the principles of medical ethics of the AMA, contain provisions declaring that the payment by or to a physician solely for the referral of a patient is fee splitting, and is unethical. This also applies to clinics, laboratories, hospitals or other health care facilities. (See Opinions 6.02, 6.03).

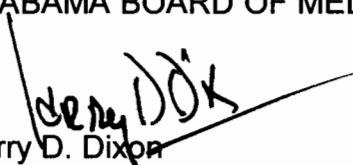
In addition, §34-24-360(10), Code of Alabama 1975, provides that a physician's license may be disciplined by the Medical Licensure Commission for the "Division of fees or agreement to split or divide the fees received for professional services with any person for bringing or referring a patient." This section of the Medical Practice Act has not been interpreted by the appellate Courts. The State Board of Medical Examiners, as the investigative and prosecutorial agency for physicians licensed in Alabama, would be required to interpret the provisions of §34-24-360(10) to determine whether a physician's conduct fell within the prohibitions of the aforementioned section and warranted the filing of an administrative complaint before the Medical Licensure Commission. The Medical Licensure Commission of Alabama has final authority to determine whether a violation of the provisions of §34-24-360 has occurred.

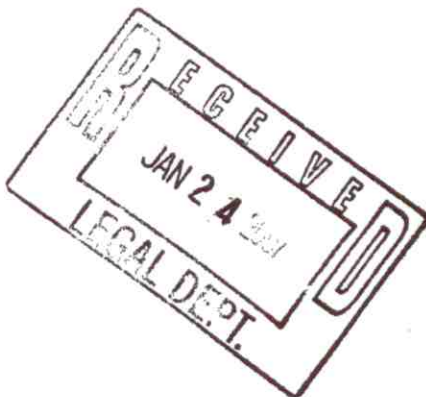
In applying the provisions of the aforementioned section of the Alabama Code to the factual situation described above, the Board has concluded that the contractual arrangement between the Laboratory and the Urology Group does not constitute a violation of §34-24-360(10). This Declaratory Ruling is limited to the facts stated herein and is not binding on the Medical Licensure Commission of Alabama.

I hope that the foregoing information is responsive to your request.

Sincerely,

ALABAMA BOARD OF MEDICAL EXAMINERS

  
Larry D. Dixon  
Executive Director



Richard L. Sharff, Jr.

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January 22, 2007

**VIA U.S. MAIL**

Alabama State Board of Medical Examiners  
Larry D. Dixon, Executive Director  
848 Washington Avenue  
Montgomery, AL 36104

Dear Mr. Dixon:

John Hogan, an attorney with Stevens & Lee, P.C., and I represent a fully-licensed independent pathology practice that provides a full range of technical and professional anatomical pathology services to its physician clients (the "Laboratory"). The Laboratory proposes to enter into a contractual arrangement, as described below, with a professional association of urologists licensed to practice medicine in Alabama (the "Urology Group"), for the provision by the Laboratory of certain pathology services to the Urology Group.

The Laboratory is requesting from the State Board of Medical Examiners (the "Board") a declaratory ruling on the propriety of the proposed arrangement. More specifically, the Laboratory seeks clarification as to the applicability of § 34-24-360(10) of the Code of Alabama to the proposed arrangement.

**Factual Background**

The Laboratory and the Urology Group desire to enter into a written services agreement under which the Laboratory would provide to the Urology Group both the technical component and the professional component of anatomical pathology with respect to certain specimens delivered from time to time by the Urology Group.

The Urology Group would bill third party payors (and/or patients when applicable based on relevant copays, deductibles or cash-paying patients) for all such services, and would retain any and all amounts collected with respect to such billings. The Laboratory would provide services under the agreement only in connection with private pay patients and those patients who are covered by commercial or private health insurance plans. The proposed arrangement would not relate to pathology services provided to patients covered by Medicare, Medicaid or any other federal or state health care program.



As payment for services rendered, the Urology Group would pay the Laboratory a fee in an amount equal to a fixed percentage of the sum collected by the Urology Group. The fee would be negotiated at arm's length and would be set at a level that would constitute fair market value compensation to the Laboratory. The fee would be established in advance of the provision of any services, would remain unchanged for the duration of the initial one-year term of the agreement, and would be subject to renegotiation only in connection with annual renewal of the agreement.

We note further that the fee would be established without regard to volume or value of referral by the Urology Group of federal health care program business to the Laboratory, and without regard to whether the Urology Group refers any federal health care program business, or any other business not covered by the agreement, to the Laboratory.

The level at which the fee would be set would anticipate a volume of work by the Laboratory based on the historical need of the Urology Group for anatomical pathology services. But, the percentage would not change during the one-year initial term or any one-year renewal term, even if the Urology Group's workload proved to be less than anticipated, or if the Urology Group chose to purchase less than the historical volume of such pathology services from the Laboratory.

In other words, the Urology Group would not be required to purchase any minimum volume of services from the Laboratory. The proposed arrangement would be non-exclusive, in that the Urology Group would be free to obtain pathology services from any person or entity of their choice, and the Laboratory would be free to offer its technical and professional services to any other person or entity. The Urology Group would make a profit from the arrangement, but the percentage fee agreed upon by the parties would provide to the Laboratory a fair market value profit from its provision of pathology services.

#### **Background – Prior Board Decisions**

In an August 5, 2004 Declaratory Ruling (the "2004 Ruling"), the Board concluded that "a discount for professional services provided to a patient's attending physician by a company offering pathology services under a billing arrangement which permits the treating physician to bill the patient (or the patient's third party payor) an amount greater than that actually paid by the attending physician for which no additional services were provided constitutes the division of fees or an arrangement to split or divide fees for professional services for bringing or referring a patient within the meaning of Ala. Code § 34-24-360(10)."

The Board clarified the applicability of the 2004 Ruling in an October 24, 2005 Declaratory Ruling (the "2005 Ruling"), in which a pathology group practice and a group of urologists proposed to enter into a professional services agreement, under which the pathology group would make its pathologists available to provide anatomical pathology services to the urology group's patients. In return, the urology group would pay a flat monthly fee that had been arrived at based in part upon the anticipated workload of the pathologists; provided that the parties' good faith estimate of the anticipated workload was not materially low, the payment to the pathology group would exceed its costs to provide the services. In that case, the Board

concluded that the payment of a flat fee would not violate the prohibition under § 34-24-360(10) on splitting or dividing fees for professional services in exchange for referring a patient.

In the 2005 Ruling, the Board declined a request to opine on the permissibility of a structure in which the Urology Group would pay the Laboratory a fixed percentage of the Urology Group's collections with respect to the services rendered by the Laboratory. The Board did so based on the fact that it was already opining in an affirmative manner on alternate grounds (*i.e.*, the flat fee approach) with respect to the proposed arrangement.

In a March 31, 1988 Declaratory Ruling (the "1988 Ruling"), the Board evaluated a contractual relationship between a group of licensed ophthalmologists and a licensed pediatric ophthalmologist, pursuant to which the pediatric ophthalmologist would provide medical services to the group in exchange for a fixed percentage of the fees generated by the ophthalmologist. *See Alabama State Board of Medical Examiners to W.M. Hughes, March 31, 1988.* Importantly, the Board found that the arrangement was acceptable under § 34-24-360(10), provided that the percentage retained by the medical partnership was reasonably related to the cost of furnishing facilities and services to the independent contractor. The Board further opined that in order to establish a violation of § 34-24-360(10), it would be necessary to demonstrate that the compensation given or received was directly related to the referral of a patient.

#### Analysis

We submit that the proposed arrangement would not violate §34-24-360(10) because the proposed arrangement is substantially similar to the arrangement described in the 1988 Ruling and should be treated in the same manner.

In both cases, the parties proposed to enter into an independent contractor relationship under which medical services would be provided in return for a fixed percentage of the collections resulting from such provision of services.

In both cases, the percentage retained or paid would be reasonably related to the costs incurred by the party retaining or receiving the fee.

In both cases, the rate of compensation paid would not be related to the referral of a patient. With respect to the proposed arrangement, the Urology Group would instead compensate the Laboratory for pathology services at a rate based upon an evaluation of the costs of providing such services, negotiated between the parties at arm's length.

In short, the Laboratory would be compensated based on a fixed percentage of the revenue generated in connection with pathology services actually rendered, and that percentage would be reasonably related to the actual estimated costs associated with the services, based on relevant historical data, and would equal the estimated fair market value of the pathology services. Consistent with the 1988 Ruling, such an arrangement should be viewed as permissible under §34-24-360(10).



We greatly appreciate the Board's consideration of this request. I am available to answer any questions and to provide any clarification.

Sincerely,

Rich Sharff  
Richard L. Sharff

cc: A. Lester Hayes, Esq.  
John M. Hogan, Esq.

Richard L. Sharff, Jr.

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February 26, 2007

**VIA FACSIMILE AND U.S. MAIL**

Alabama State Board of Medical Examiners  
Attn: A. Lester Hayes, Esq.  
848 Washington Avenue  
Montgomery, AL 36104

Dear Les:

I am following up on your recent question to me about my January 22, 2007 letter to Mr. Larry Dixon requesting a declaratory ruling from the State Board of Medical Examiners (the "Board") on the propriety of a proposed arrangement between my client, a fully-licensed independent pathology practice (the "Laboratory"), and a professional association of urologists licensed to practice medicine in Alabama (the "Urology Group"), for the provision by the Laboratory of certain pathology services to the Urology Group.

As described in more detail in my January 22 letter, under the proposed arrangement the Urology Group would bill payors for the Laboratory's anatomical pathology services and pay the Laboratory a fee in an amount equal to a fixed percentage of the sum collected by the Urology Group. The percentage fee would be negotiated at arm's length and would be set at a level that would constitute fair market value compensation to the Laboratory. The fee would be established in advance of the provision of any services, would remain unchanged for the duration of the initial one-year term of the agreement, and would be subject to renegotiation only in connection with annual renewal of the agreement.

As I understand it, you asked if I could comment on whether the percentage retained by the Urology Group would be reasonably related to its cost of furnishing billing and any other services provided by the Urology Group in connection with the arrangement. The answer to that question is no, but I believe that the reason for my client's inability to answer that question actually reinforces our position that the proposed arrangement is legal and does not violate Ala. Code § 34-24-360(10).

The Laboratory sets its fixed percentage fee based upon its own costs and reasonable profit expectations, and that fee is not negotiated with the various physician practices that obtain the Laboratory's services. In other words, the Laboratory maintains a set fee schedule for all of

its clients across the country. The Laboratory neither knows about nor concerns itself with the extent to which the physician group profits from the arrangement, which will vary depending upon the particular group's costs in connection with the arrangement and reimbursement rates from payors. We believe that these facts further demonstrate that the purpose of the percentage fee arrangement is to ensure that the Laboratory is paid a fair, market-based price for its services, and not to improperly "split fees" with the physician groups that elect to purchase those services.

I hope this additional information helps the Board respond to our request. Of course, if I have misinterpreted your question, or you have additional questions, please do not hesitate to call me again.

Sincerely,

  
Richard L. Sharff

cc: John M. Hogan, Esq.