

Exceptions and Alternatives to The Corporate Practice of Medicine

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While most states prohibit the corporate practice of medicine, many do have exceptions. Physicians need to understand which working relationships – with hospitals, other physicians, and with non-physicians – are permitted. Health care ventures that do research or provide ancillary medical services need to understand when their work might violate the corporate practice of medicine laws.

An experienced health care lawyer will review the current laws and regulations. He'll also help you explore and develop alternatives that may be permissible.

The status of corporate practice of medicine laws

Most states allow for corporations to hire physicians if physicians own the corporation – the essence of a professional medical corporation. Some states allow certain government, nonprofit, and corporate entities to hire physicians. According to a [California Senate study](#), 28 states permit hospitals to hire doctors. 30 states give physicians the right to operate a medical practice as a limited liability company.

The three states with the most robust bans against the corporate practice of medicine and the prohibition against the hiring of physicians (outside of limited exemptions) are California, Colorado, and Iowa. Many states that do have bans against the corporate practice of medicine include dentists in the ban.

Exceptions to the California prohibition against the corporate practice of medicine

There are some direct exceptions to the California laws that prohibit the corporate practice of medicine, such as creating a professional medical corporation. There are also strategies that can be used such as the use of a management services organization (MSO) to help ensure that the medical practice meets its financial needs while also ensuring that the care and treatments of patients is the priority.

Aside from professional medical corporations, the entities that generally use an exception to the prohibition against the corporate practice of medicine in California are either nonprofits or government organizations.

Generally, both nonprofit hospitals and hospitals owned by healthcare districts are subject to the ban. Conversely, medical school health systems, which sometimes compete with nonprofit and for-profit hospitals, are not subject to the ban.

What Physicians and Investors Must Know About California Medical Corporations

Doctors must comply with California's Professional Corporation Act. A professional medical corporation provides many advantages over a partnership or sole proprietorship.

Exemption for Professional Medical Corporation

The California Senate California Research Bureau prepared a document called *"The Corporate Practice of Medicine in a Changing Healthcare Environment"* in 2016. The research discussed some of the exemptions to the California Practice of Medicine Law. One key exemption many doctors are now using is the Moscone-Knox Professional Corporation Act. Passed in 1968, Section 12400-13410 provides one exemption to the prohibition of the corporate practice of medicine. The exemption is common (though there are differences) in many other states.

The law permits physicians, dentists, and lawyers to create professional corporations. Doctors, based on the act, can create professional medical corporations. The law was enacted to comply with the requirements of the Internal Revenue Service.

To qualify for professional medical corporation status, the professional corporations must, in general, be engaged in providing medical services for a single profession. For example, doctors and lawyers, still *"cannot serve as shareholders, officers, directors, or professional employees of each other's corporations."*

The Moscone-Knox Law, however, exempted medical professions. This means that *"license holders in a variety of other health professions can also serve as shareholders, officers, directors, or employees of professional medical corporations. These include podiatrists, psychologists, nurses, optometrists, marriage and family counselors, clinical social workers, physician assistants, chiropractors, acupuncturists, naturopathic doctors, professional clinical counselors and physical therapists."*

Exemption for Clinics and Hospitals Operated for the Purpose of Medical Education

The Senate research document states that the original law, which was clarified in an appellate court decision, indicates that medical schools are not *"subject to the corporate ban even if they are in competition with nonexempt organizations"* – since every patient is a teaching case even though the patient may not *"be seen by an intern, resident or other trainee."*

Exemption for Nonprofit Community Clinics

"A community clinic is a clinic operated by a tax-exempt nonprofit corporation that is supported and maintained by donations, grants, and government funds." Generally, the patient pays for the services according to the patient's ability to pay.

Exemption for Nonprofit research clinics

These entities are licensed by the California Department of Public Health. Nonprofit research clinics research medical diseases such as heart disease and prostate cancer. These clinics generally only provide care to patients through the results of their research. Clinics may generally hire doctors and charge for their professional services. A clinic *"shall not interfere with, control, or otherwise direct the professional judgment of a physician and surgeon in a manner prohibited by Section 2400 or any other provision of law."*

Exemption Licensed charitable institutions, foundations or clinics

Pursuant to 16 California Code of Regulations, Section 1340, the Medical Board of California permits any licensed charitable institution, foundation or clinic to employ physicians and surgeons so long as the entity does not charge for professional medical services. In such a case, the physician or surgeon would directly bill the patient or the insurance company.

Additional exceptions

Other entities that may qualify for exempt status include:

- County hospitals
- State agencies
- Nonprofit research clinics
- Specialty pediatric hospitals
- Other medical entities

Generally, according to the California Senate study, HMOs are exempt from California's ban on physician employment, (based on the federal Health Maintenance Organization Act of 1973). California's Knox-Keene Act allowed HMOs to hire physicians if the HMO model was a staff model. Most HMOs are not staff models. Most HMOs are group or independent practice association models.

Stark law and the hospital/physician employment exception

In states where hospitals can hire physicians (under broad exceptions like many states or limited exceptions such as in California) there is another roadblock to the hospital/physician employment contract that must be addressed. Stark Law was enacted to ensure that patients weren't being referred to a designated healthcare facility (such as hospital) because the physician was receiving a referral fee or benefit. Referrals should be made to hospitals based on the best interest of the patient and not the financial interest of the doctor.

Recent Stark Law and Anti-Kickback Statute Cases

Medical providers must abide by Stark Law and the AKS. Referrals must be based on what is best for the patient. If profit is the driver, the providers will often pay a substantial settlement or [...]

There are many exceptions to Stark Law including the physician employment contract – provided the terms of the Stark exception are met. An experienced Stark Law attorney can help draft the appropriate contracts. Stark law requires that the employment contract between the hospital and physician be a “*bona fide employment relationship*.” This means that any sums paid by the hospital to the doctor (or an immediate family member) who has a bona fide employment contract with the hospital for services may be allowed if the following conditions are met:

- The employment is for specific identifiable services
- The amount being paid under the employment contract should:
 - Align with the fair market value for those services
 - With limited exceptions, should not be based (indirectly or directly) on the volume of any referrals by the referring doctor.
- The payment/remuneration should be “*provided under an arrangement that would be commercially reasonable even if no referrals were made to the employer.*”
- A payment may be acceptable if the payment is in the form of a productivity bonus.

Stark law has a separate section which sets forth when and how hospitals can use remuneration payable to the physician in order to recruit physicians to relocate their medical practice to a geographical area serviced by the hospital.

The Anti-Kickback Statute and the hospital/physician safe harbor

The AKS statute was enacted to ensure the integrity of the healthcare professions. The law prohibits the payments of kickbacks or inducements to encourage or pressure physicians to make referrals based on economic incentives instead of doing what's best for the patient. In states that permit hospitals or clinics to hire physicians, the hospital and doctor must still comply with the AKS.

Violations of the law can result in criminal charges and civil lawsuits. The AKS does have a safe harbor which an experienced healthcare lawyer can explain. One safe harbor that applies to hospital/physician employment is the safe harbor for *"personal services and management contracts."* This safe harbor can help protect the hospital/doctor employment contract if:

- The agreement is set forth in writing and signed by the hospital and physician.
- The contract covers all the services the physicians will provide to the hospital.
- The contract provides the details as the length and schedule of services and the charges – if the arrangement is not for full time work,
- The agreement should be for one year or more.
- The combined compensation to the physician should be consistent with fair market value and shouldn't be based on the volume or value of referrals between the hospital and doctor – *"for which payment may be made in whole or in part under Medicare, Medicaid or other Federal health care programs."*
- The contract shouldn't violate state or federal law
- The total services shouldn't be more than what are *"reasonably necessary to accomplish the commercially reasonable business purpose of the services."*

As with Stark Law, the AKS safe harbor includes physician recruitment issues.

The management services organization (MSO) – a practical exception

In California, and other states, the managed service organization can be a useful way to address concerns about the corporate practice of medicine, Stark Law, and the Anti-Kickback Statute.

An MSO is a way for non-physicians to own a management services organization (MSO) which is specifically designed to run the administrative and non-medical parts of the medical practice. An MSO is a way for physicians to focus on the business side of their medical practice while working to avoid any conflict with the independent medical judgment of the physicians.

As we discussed in our article on when an MSO is the right choice for a medical practice, an MSO can *"buy the assets of a practice (to provide capital) and then offer the practice essentials such as equipment or space."* The MSO can provide a range of services including:

- Educating and training staff
- Payroll and medical coding
- Managing equipment
- Office rental
- Staff credentials
- The information technology side of the business
- Marketing and sales
- Disaster management
- Insurance

- Many other non-medical judgment issues

It is critical that the doctors not cede too much control to the MSO. If physicians do cede too much control, then these health providers may violate California's (or another state's) prohibition against the corporate practice of medicine.

When Using a Management Services Organizations (MSO) Is the Right Choice for Your Medical Practice

Managed Services Organizations help physicians focus on practicing medicine by freeing doctors from many administrative tasks. Failure to consult with an MSO healthcare lawyer can cause civil and [...]

An experienced healthcare lawyer can explain what exceptions to the corporate practice of medical laws apply and whether any of those exceptions can be used for your practice or your health venture. Even when health providers can pass the corporate practice of medicine test, there are other hurdles that must be addressed to such as fee-splitting and improper referrals – which are monitored by Stark Law and the Anti-Kickback statute. An MSO is a common strategy for separating the business functions of a medical practice from the business functions.

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