Are your Leases Compliant with the "Stark III" Regulations?

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Siebers Mohney Blog
April 15, 2008

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Are you a physician renting medical office space in a complex owned by a hospital with whom you have a referral relationship? Do you have a lease with another provider with whom you have a referral relationship where space or equipment is shared? The long-anticipated Phase III final rule took effect December 4, 2007. However, I have found that many providers--and even their attorneys--are not aware of, or seemingly unconcerned with, the regulations as they affect leases. The Stark regulations impose strict requirements upon leases. Therefore, if a provider is attempting to fit within the narrowly-interpreted lease exception to the anti-referral prohibition, a lease amendment may be necessary. The rental of office space exception provides that a prohibited financial relationship excludes payments for the use of office space if:

1. There is a written agreement, signed by the parties, specifying the space covered by the lease;
2. The term of the lease is at least one year. If the agreement is terminated during the term with or without cause, the parties may not enter into a new agreement during the first year of the original term of the agreement;
3. The space leased is reasonable and necessary for the legitimate business purposes of the lease;
4. The space leased is used exclusively by the lessee when being used by the lessee, but the lessee may make payments for the use of the space consisting of common areas if the payments do not exceed the lessee's appropriate pro rata share of expenses;
5. The rental charges are set in advance, consistent with fair market value;
6. The rental charges are not determined in a manner that takes into account the volume or value of any referrals or other business generated between the parties;
7. The lease agreement would be commercially reasonable even if no referrals were made between the lessee and the lessor; and

8. A holdover month-to-month rental for up to 6 months immediately following the expiration of an agreement that met the conditions of this exception satisfies the exception if the holdover rental is on the same terms and conditions as the immediately preceding agreement.

A similar exception also exists for the rental of equipment.

The Stark III final rule does not make any substantive changes to the space and equipment lease exceptions as adopted in Phase II. However, what is most notable to me is the exclusivity requirement. The lessee must have exclusive use of the space or equipment when using it. Most commentators are interpreting this to require "block leases", where the lease includes clearly delineated blocks of time for each party to exclusively use the space. Therefore, if an exam room is used by two parties, they will need to determine at what times of the day or week each party will have exclusive use of it.

In the commentary to Stark III, many commenters pointed out that "sharing of facilities is extremely common for physicians and may not readily fit into the leasing exceptions. CMS' response was: "Irrespective of whether the office-sharing arrangements described by the commenters are common, both the statute and our regulations require that the lessee have exclusive use of the leased space or equipment when the lessee uses the space or equipment. In effect, [these exceptions] require that space and equipment leases be for established blocks of time."

Also, subleases are allowed. The commentary notes that a lease (or sublease) is considered to satisfy the "exclusive use test" provided that the lessee (or sublessee) does not share the rented space or equipment with the lessor during the time it is rented or used by the lessee (or sublessee). However, CMS correctly points out that "a subleasing arrangement could create a separate indirect compensation arrangement between the lessor and a sublessee that would need to be evaluated under the indirect compensation rules."

This exception contains some defined terms not elaborated on here, and also will affect certain lease amendments, as may other provisions in Stark III.

At the end of a busy shift providing medical services, the last thing a physician will probably feel like doing is pulling out and studying her or his lease agreement. However, since the regulations stem from a strict liability statute imposing harsh civil monetary penalties and possible disciplinary action under Michigan licensing laws, it is better to be safe than sorry and have an attorney review your lease to ensure compliance.