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an agreement under which the physician leases or has a role in leasing equipment from or to a laboratory.

Response: We agree with the commenter that, if a physician who is leasing equipment from a laboratory under controlled circumstances refers to that laboratory, this should not lead to program or patient abuse. Section 1877(e)(1)(B), which was added by OBRA '93 retroactive to January 1, 1992, excepts from "compensation arrangements" payments made by a lessee of equipment to the lessor for the use of the equipment if certain conditions (discussed earlier in this preamble at section I.D.7.b.) are met. These conditions are specified in § 411.357(b) of this rule.

5. Group Practice Affiliated Property Companies

In the impact analysis of the proposed rule (57 FR 8601), we discussed group practices with affiliated property companies that are owned by members of the group practice and that lease facilities or equipment to the group. We stated that the group practice would need to restructure if it wanted to continue to make Medicare referrals for clinical laboratory services. Technically, we regarded the lease of equipment by the property company to the group practice that operates a clinical laboratory as a compensation arrangement for which an exception was not provided in the proposed rule. In these cases, it was indicated that the prohibition on referrals would apply, which would require the group physicians to either purchase the equipment from the property company or divest their interests in the laboratory if they intended to continue to make Medicare referrals for clinical laboratory services.

Comment: According to one commenter, in some group practices, affiliated property companies serve as the vehicle for the retirement system for the equity partners in the group practice; that is, as vehicles for creating retirement income. This commenter recommended that we provide an exception for group practices that have affiliated property companies under circumstances in which there is no potential or incentive for program or

Response: What this commenter is concerned about is that the compensation arrangement between the affiliated property company and the group practice might prohibit referrals by the physicians of the group practice to their own in-office laboratory. In this situation, one or more of the group practice physicians who own the

property company receive remuneration from the group practice. In the impact analysis of the proposed rule (57 FR 8601), we indicated that a group practice probably would have to divest its interest in an affiliated property company if it intended to refer Medicare patients to its in-office laboratory. After reconsidering the matter, however, we do not believe that our initial interpretation was correct.

Section 1877(a)(1) of the Act prohibits a physician from making referrals to an entity that furnishes clinical laboratory services if the physician or immediate family member has a financial relationship with that entity. In the situation described by the commenter, the group practice physicians appear to have a financial relationship with the affiliated property company which rents equipment to their laboratory, in the form of an ownership interest. We also regarded as a compensation arrangement the payments which the group practice makes to the affiliated property company for renting the equipment. However, the physicians in this case do not have these financial relationships with an entity that furnishes clinical laboratory services; their relationships are with an entity that only rents equipment to the group practice. As a result, these relationships with the affiliated property company should not affect the physicians' ability to refer to their own laboratory.

Instead, the group practice physicians' referrals could be prohibited because they are referring to a laboratory that they own. Section 1877(b)(2) provides an exception for group practices which refer Medicare patients to their own laboratory for in-office ancillary services. These services must be furnished personally by a member of the group practice or an individual who is directly supervised by a member of the group practice, provided these services are furnished in the building where the group practice has its office or a building that is used by the group practice for furnishing some or all of the group's clinical laboratory services. This provision also has certain billing requirements. The conditions in this exception do not place limitations on the origin of the laboratory equipment that is used by the group practice.

Thus, we have determined that, if the in-office laboratory services are furnished in the manner described by section 1877(b)(2) and § 411.355(b), the nature of the physician's financial relationship with the in-office laboratory is irrelevant. As a result, we do not believe that an additional exception is necessary.

6. Faculty Practice Plan Exception

Comment: Several commenters suggested that a separate exception be developed to treat faculty practice plans associated with accredited medical schools as a separate and distinct type of group practice. These commenters indicated that it is not uncommon in a faculty practice plan environment for the physicians to receive their compensation from one entity (the medical school, for example). However, they may conduct their practice through a separate entity that might be a professional corporation, partnership, or simply a contractually organized billing service. In addition they may order their laboratory work from one or more related entities (for example, the teaching hospital, the university's research laboratory for highly specialized testing, in-office laboratories within faculty departments that may or may not be incorporated as professional corporations, etc.). Since there is no consistent organizational arrangement that characterizes a faculty practice plan, these commenters requested that we develop a separate provision that would treat faculty practice plans associated with accredited medical schools as a separate and distinct type of group practice. They have suggested that the definition of a group practice and the separate requirements of the inoffice ancillary exception be applied at the level of the umbrella organization. That is, they believed each legal entity within the same academic setting should not be required to satisfy these provisions. In this manner, any physician who is a staff member of the umbrella organization would be permitted to refer Medicare patients to laboratories that are owned or operated by the umbrella organization.

Response: We believe that the amendments made by OBRA '93 make an additional exception unnecessary. We acknowledge that faculty practice plan physicians may be associated with many organizations in an academic setting, in terms of receiving compensation, furnishing patient care, teaching, and doing research. For example, the medical school may pay the plan to teach residents or care for patients. Even though faculty practice plans may operate in a variety of arrangements, the common theme appears to involve physicians or groups of physicians who are compensated by some part of an academic center for providing a variety of services, and who are concerned about whether they can refer patients to laboratories that belong to the academic center.