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**Vendor Contracts:
Compliance is a Three-Way Street**

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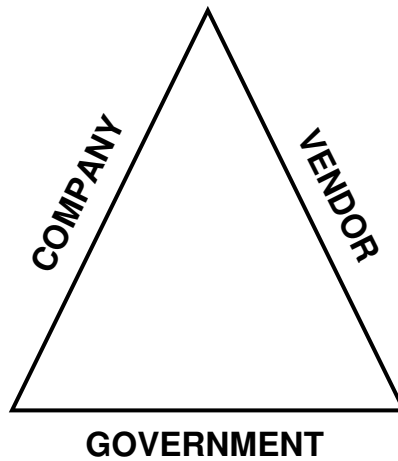
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All Three Entities are Interrelated



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Key Outlooks

- Government – protect healthcare programs by not overpaying for services, and protect consumers by regulating products/services.
- Company – procuring goods and services at known and agreed upon prices. Looking for right combination of quality product, quality service, and price.
- Vendor – generate sales, retain customers, and maximize profits.



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Key Risks

- Government
 - Overpayments for services participants received
 - Overpayments for services participants did not receive
 - Quality services not received by participants
 - Physicians/participants induced to receive additional services: questionable medical necessity



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Key Risks (continued)

- Company
 - Overpayments to vendors (pricing and credit memos)
 - Underpayments from vendors (GPO fees and rebates)
 - Inability to drive volumes increases costs
 - Physician preference
 - Vendor “sales pitches”/inducements
 - Failure to allocate savings to government programs



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Key Risks (continued)

- Vendor
 - Declining sales
 - Losing customers
 - Deteriorating margins
 - Inappropriate activities/tactics by sales force
 - Expiring patents
 - Competition



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Approaches

- Government
 - FDA
 - Drugs
 - Implants
 - TJC (JCAHO)
 - Equipment Service Records
 - Anti-kickback statute
 - GPO safe harbor (42 C.R.F. 1001.952(j))
 - Written agreement
 - 3% or less fee on purchase price
 - False Claims Act
 - Cost reports



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GPO Fees

“Although they provide a service to hospitals, most GPO’s are private, for-profit companies. Because they are funded by administrative fees calculated as a percentage of the contracts they negotiate, higher prices for supplies mean higher profits for GPO’s – a major flaw in the scheme, since it effectively puts the interests of GPO’s at odds with the interests of the hospitals they’re supposed to be helping. Money left over after GPO’s pay operating expenses is supposed to go back to the member hospitals. This arrangement was sanctioned by the 1986 bill passed by Congress, giving the GPO’s “safe harbor” from kickback laws. The theory was that passing the GPO’s operating costs to suppliers would help hospitals’ financial bottom lines. Administrative fees were capped at 3% of a contract’s value – anything above that is supposed to be scrutinized for fraud by CMS.”

Fort Worth Weekly Feature: Wednesday, October 4th, 2007. By: Pablo Lastra



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Approaches (continued)

- Company
 - Participate in GPO's
 - Volume pricing
 - Excess GPO fees
 - Quality Committees
 - Reduce variation of equipment/supply purchases
 - Restrict vendor representative access to hospital areas
 - Good contracting processes
 - Good accounting processes and cost allocation procedures
 - Employee education
 - Internal audits



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Approaches (continued)

- Vendor
 - Focus sales efforts: physicians, consumers, customer “champions”
 - GPO fees, versus pricing, drives volumes
 - Employee education
 - Lobby government to extend patent protection
 - New uses of existing technology
 - Rapidly changing technology (obsolescence)



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Company Vendor Audits

1. Assess contract process
 - a. Basis: bid, negotiate, etc.
 - b. Who performs
 - c. Conflicts of interest?
2. Determine which contract(s) will be audited (risk-based)
3. Read contracts for understanding: duties and responsibilities of parties
4. Define audit scope
5. Assess risks related to scope
6. Verify propriety of membership lists
7. Obtain sales volumes/purchases under contract
 - a. Internal data
 - b. Vendor data



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Company Vendor Audits (continued)

8. Recalculate GPO fee (contracted, not to exceed 3%) based on volumes
9. Verify GPO fee paid correctly
10. Verify GPO fees received in excess of GPO expenses “returned” to partners/facilities
11. Verify “returned” GPO fees allocated to appropriate cost centers
12. Recalculate rebates
13. Verify rebates allocated to appropriate facilities
14. Verify rebates allocated to appropriate cost centers
15. Test credit balances
 - a. How much
 - b. How old



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Company Vendor Audits (continued)

16. Test pricing (actual vs. contract)

- a. Universe
- b. Sample
- c. Extrapolation
- d. Tier pricing
- e. Impact on rebates and GPO fees

17. Other issues

- a. Freight "handling" subject to sales tax in some states
- b. Fill rates: penalties resulting in additional rebates
- c. Failure to supply: penalties resulting in additional rebates



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Questions/Discussion



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