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**Subject: *Health System Leases and Off-Campus Space Agreements
Report 2016-49***

The final report for *Health System Leases and Off-Campus Space Agreements, Report 2016-49*, is attached. We would like to thank all members of the department for their cooperation and assistance during the review.

Because we were able to reach agreement regarding management action plans in response to the audit recommendations, a formal response to the report is not requested. The findings included in this report will be added to our follow-up system. We will contact you at the appropriate time to evaluate the status of the management action plans.

UC wide policy requires that all draft reports be destroyed after the final report is issued. We also request that draft reports not be photocopied or otherwise redistributed.

David Meier
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Attachment

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UC San Diego

AUDIT & MANAGEMENT ADVISORY SERVICES

Health System Leases and Off-Campus Space Agreements

Report No. 2016-49

May 2016

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I. EXECUTIVE SUMMARY

Audit & Management Advisory Services (AMAS) has completed a requested review of Health System Leases and Off-Campus Space Agreements as a supplemental audit on the Fiscal Year (FY) 2015-16 audit plan. The objective of our review was to evaluate whether controls for Health Sciences tenant lease agreements and other agreements for use of off-campus space provided reasonable assurance that processes were effective, and agreements are properly executed in accordance with University policy.

We concluded that processes for executing clinical partnerships and service agreements which include a space component could be improved to provide better assurance that space and facility considerations are evaluated prior to execution of the agreement to mitigate business, regulatory, and compliance risk. The broad delegation of authority to the UCSD Health (UCSDH) Chief Executive Officer and School of Medicine (SOM) Chief Operating Officer (COO) allowed for the execution of these agreements, however we noted that processes did not consistently ensure that Real Estate Development (RED) was appropriately involved in the evaluation of terms relating to space prior to the agreement being executed. RED involvement is important to ensure terms relating to space are appropriate and protect University interests, and that pricing for space is at fair market value. A more consistent process could also ensure that Facilities Management (FM) evaluation of space from a regulatory and safety perspective could occur prior to agreement execution. The Management Action Plan to address this finding is summarized below:

A. Evaluation of Space for Clinical Partnerships and Service Agreements

The Health System Strategy Office will implement a process to ensure collaboration with RED on space issues for all new agreements. The Strategy Office is in process of developing a standard checklist to serve as a guide for this process, which will include review of agreements with both RED and FM. For existing agreements, collaboration on terms will be performed at the time of agreement renewal.

Observations and the related Management Action Plan are described in greater detail in section V. of this report.

II. BACKGROUND

Audit & Management Advisory Services (AMAS) has completed a requested review of Health System Leases and Off-Campus Space Agreements as a supplemental audit on the Fiscal Year (FY) 2015-16 audit plan. AMAS was requested by the UC San Diego Health (UCSDH) Chief Compliance, Privacy, and Risk Officer to evaluate whether lease agreements may exist which were not processed through the Campus Real Estate Development (RED) office and may not have received full due diligence and analysis for appropriate terms, conditions, and pricing. This report summarizes the results of our review.

UCSD Policy & Procedure Manual (PPM) 440-3 *Leased Real Property* designates the RED Office as the responsible office for all off-campus leased space. The policy requires that all requests or inquiries regarding leasing property from external entities must be directed to RED. Further, no commitment may be made on behalf of the University, except by persons having formal delegations of authority for real property contract execution. PPM 440-3 outlines the importance of RED involvement in lease agreements to

“ensure (i) appropriate approvals to proceed with leasing space off-campus are received; (ii) coordination of inspections conducted by UCSD’s Environment, Health & Safety (EH&S) and Facilities Design & Construction (FD&C) is completed; (iii) all financial and business negotiations with external entities are conducted by Real Estate Development; (iv) an evaluation of fair market rents is completed; (v) appropriate approvals on the Standard Form Lease Agreement (SFLA) are obtained; and (vi) leased space is delivered to the department in a timely and satisfactory manner.”

This policy is supported by a Delegation of Authority from the Chancellor to the Vice Chancellor-Chief Financial Officer, which is further re-delegated to the Executive Director, Real Estate Development, for “the authority to negotiate and ..., to approve and execute licenses of real property including facilities use agreements and other forms of agreement that are equivalent to licenses of real property (except those licenses relating to real property held as an investment of the Corporation), when such agreements: 1. Involve: (i) real property that is or will be used for University-related purposes, or (ii) University-related real property to be used by others, and (iii) are limited in the length of term and consideration...”

Leases in the healthcare environment require careful review to ensure that terms do not raise concerns under federal Physician Self-Referral (“Stark”) law¹ or Anti-Kickback Statute². Under Stark law, leases must comply with the following requirements:

- Lease must be in a written agreement signed by the parties, and specify the premises covered by the lease;

¹ 42 U.S.C. § 1395nn. Generally, this law Prohibits a physician from referring Medicare patients for designated health services to an entity with which the physician (or immediate family member) has a financial relationship, unless an exception applies, and prohibits the designated health services entity from submitting claims to Medicare for those services resulting from a prohibited referral.

² 42 U.S.C. § 1320a-7b(b). Generally, this law prohibits offering, paying, soliciting or receiving anything of value to induce or reward referrals or generate Federal health care program business.

- The space can not exceed that which is reasonable and necessary for the legitimate business purposes and may include proportional space allocation of common areas;
- Leases must have a term of at least one year;
- Rent charges are set in advance, are consistent with fair market value, and are not determined in a manner that takes into account the volume or value of any referrals or other business generated between the parties; and
- The lease would be reasonable even if no referrals were made between the parties

In addition to a Real Property Lease, other types of contract vehicles may include consideration for space in which the University provides clinical or professional services. For example, the UCSDH Chief Executive Officer (CEO) has broad delegated authority for the operations of the UC San Diego Health System. This includes developing plans for quality patient care services, which may be accomplished through agreements with community partners. Agreements approved by the CEO may include Joint Ventures, Management Service Agreements, and other strategic partnerships. These agreements are processed through the UCSDH Strategy Office.

Also, the School of Medicine (SOM) Assistant Dean / Chief Operating Officer (COO) has delegated authority from the Chancellor to “execute the various service agreements required with outside organizations, agencies, and individuals to implement approved programs and activities relating to the School of Medicine whether the University is the supplier or recipient of the service covered by the agreement.” These agreements, commonly known as Service Agreements, can be for professional medical or patient care activities or other clinical services provided by SOM Faculty. These agreements are processed through the SOM Business Contracts Office and Department Business Officers. Broadly interpreted, these agreements with outside entities, either through an executed UCSDH agreement or SOM Service Agreement, may include space, as well as the professional and staff services required to fulfill the service.

With these agreements, space is typically one of several cost factors in a broader payment structure negotiated with the outside entity. In these instances, it would be important to assure similar protections related to use of space and fair market value pricing as would be present in a formal Real Property Lease to avoid exposure under Stark law and AKS.

UC San Diego Health Facilities Management (FM) also has a role in oversight for UCSDH space. Medical Center Policy (MCP) 541.4, *Facilities & Capital Asset Management (FCAM)* states that the Director of Facilities Planning is responsible for the management of UCSDH space, including analysis of space requirements, identification of available owned or leased space, coordination of leases, maintenance of Space Inventory and Space Request Log, coordination of maintenance and alterations in leased space, and preparation of space related reports. The policy further states that Department heads are responsible for assessing departmental space needs and for communicating those needs to their respective Senior Management Team Executive. FM coordinates with departments on new space to ensure that structural, safety, and regulatory requirements are met for space occupied by UCSDH employees or patients. During the past year, a Strategic Space Committee was formed to review UCSDH department space requests. FM, RED, the Chief Administrative Officers, and others participate on this committee.

Concurrent with this review, AMAS performed an audit of Clinical Partnerships (AMAS Audit 2016-14), which included an evaluation of business processes related to one particular partnership agreement with an outside entity. Our review included observations regarding contract management processes, and as a result management agreed to develop an action plan for more consistent oversight and pre-agreement due diligence for agreements with outside entities.

Also during our review, UCSD Health System management charged a Professional Services Contract Administration Management Team (Contract Management Team) to review current contract administration processes for agreements with external entities. The team includes representatives from the Health System Strategy Office, SOM Dean's Office, select SOM Departments, and Health Sciences Compliance. This team will be evaluating processes both at the front end when negotiations begin, to the back end when agreements need to be managed and monitored, to identify and recommend improvements with the goal of developing a consistent process. AMAS participated on this team in an advisory capacity during the review.

III. AUDIT OBJECTIVE, SCOPE, AND PROCEDURES

The objective of our review was to evaluate whether controls for Health Sciences tenant lease agreements and other agreements for use of off-campus space provided reasonable assurance that processes were effective, and agreements are properly executed in accordance with University policy. In order to achieve our objective, we performed the following:

- Evaluated polices and delegations of authority related to leases, other executed agreements, and space;
- Reviewed at a high level processes for real property leases through RED, SOM service agreements, and UCSDH partnership agreements;
- Evaluated the RED Detail Active Lease (DAL) report for UC Regents as Tenants, February 2016;
- Generated an Operating Ledger Query from the Integrated Financial Information System (IFIS) for expenditures classified with account codes indicating payment of Rent;
- Compared Operating Ledger Query Results to the Health System Financial Services rent variance schedule and the RED DAL Report;
- Obtained information from the following:
 - Associate Director, RED
 - Senior Director, UCSDH Facilities Planning & Maintenance
 - SOM Associate Dean, Affiliate & Industry Affairs & Director of Business Contracting
 - UCSDH Director of Strategic Partnerships and Strategy Office Managers
 - UCSDH Chief Compliance, Privacy, and Risk Officer;
- Gathered information relating to Contract Management Team initiatives to standardize contracting processes for certain Health System and SOM agreements;
- Reviewed various listings of UCSDH and SOM agreements including off-site space, and compared locations to the DAL report; and
- Performed limited review of agreements not located on the RED DAL report.

IV. CONCLUSION

Based on our review, we concluded that processes for executing clinical partnerships and service agreements which include a space component could be improved to provide better assurance that space and facility considerations are evaluated prior to execution of the agreement to mitigate business, regulatory, and compliance risk. The broad delegation of authority to the CEO and SOM COO allowed for the execution of these agreements, however we noted that processes did not consistently ensure that RED was appropriately involved in the evaluation of terms relating to space prior to the agreement being executed. RED involvement is important to ensure terms relating to space are appropriate and protect University interests, and that pricing for space is at fair market value. A more consistent process could also ensure that FM evaluation of space from a regulatory and safety perspective could occur prior to agreement execution.

Processes for Real Property Leases for UCSDH off-campus space were generally effective. We noted that leased properties for which rent payments were processed were matched to the RED DAL inventory, indicating consistency between Real Property Leases through RED and associated UCSDH rent payments.

Additional discussion is provided in the balance of this report.

V. OBSERVATIONS REQUIRING MANAGEMENT ACTION

A.	Evaluation of Space for Clinical Partnerships and Service Agreements
Processes for executing clinical partnerships and service agreements which include a space component did not ensure review by RED prior to execution.	
Risk Statement/Effect	
Execution of agreements without review by RED exposed the University to increased risk of noncompliance with regulations and policy, terms which did not appropriately protect University assets and employees, and could increase the University’s exposure under anti-kickback laws.	
Management Action Plan	
A.1	The Health System Strategy Office will implement a process to ensure collaboration with RED on space issues for all new agreements. The Strategy Office is in process of developing a standard checklist to serve as a guide for this process, which will include review of agreements with both RED and FM. For existing agreements, collaboration on terms will be performed at the time of agreement renewal.

A. Evaluation of Space for Clinical Partnerships and Service Agreements – Detailed Discussion

Processes for executing clinical partnerships and service agreements which include a space component did not ensure review by RED prior to execution. Because there was no single central repository or listing of off-site space agreements, we evaluated information from various sources to consider whether the off-site space was negotiated by RED as a Real Property Lease, or whether RED was involved in evaluating space-related terms in agreements which were signed by other parties.

We noted a small number (seven) of cases where space was included as a component of the agreement, however RED was not involved to ensure appropriate space-related terms and pricing. One of these agreements was with a strategic affiliation partner, one related to a practice acquisition, and five were smaller agreements for part-time use of clinic space and staff. Six of the seven were signed by former UCSDH leadership, and one by the SOM COO.

Based on the results of this evaluation and information gathered via interviews, it appeared that processes for coordination between SOM Business Contracts and RED were generally effective. SOM Business Contracts advises department business officers of the need to obtain fair market value pricing from RED, and retains this information in the Service Agreement file. SOM Business Contracts also consults directly with RED as needed.

We noted that processes for evaluation of space in UCSDH agreements were historically more inconsistent. In recent years, the focus on expanding UCSDH clinical capacity through strategic partnership agreements establishment of the Strategy Office has led to increased activity in this area. Agreements are now coordinated through the Strategy Office, which works with service line leadership to review terms of the agreements. Legal review is typically performed either by UCSD Chief Health Law Counsel, the SOM Business Contracts Office, or outside counsel. In recent months, coordination between the Strategy Office and RED has improved as the Strategy Office gained experience in University requirements and best practices for execution of these agreements.

However, UCSDH agreements executed in prior years were not consistently coordinated with RED for evaluation of space terms and pricing. In particular, prior to the creation of the Strategy Office as a hub for these agreements, processes were decentralized among clinical departments or service lines, and there was not necessarily one central point of review before agreements were presented to the CEO for signature. In some agreements we identified in this review, RED was not involved in negotiation of prior to execution. These agreements were provided to RED management for additional discussion with UCSDH and/or SOM contacts as needed.

In addition to the recent increased coordination between the Strategy Office and RED, as part of AMAS Audit 2016-14, Health System Leadership is in the process of developing an action plan for consistent oversight for agreements with outside entities. Use of a checklist that identifies areas for management planning when assessing potential expansion, and the involvement of key UCSD offices in various phases of the project, will also be considered. Establishment of a more consistent process on an on-going basis will ensure that appropriate University departments, such as RED and FM, are included in evaluation of terms prior to agreement execution to mitigate University business, regulatory, and compliance risk.