

Issue Stories

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ON-LINE EXCLUSIVE: Trends and Issues

Status of Physician-Owned Hospitals in a Reformed Health Care Environment

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After almost a year of heated debate, President Obama signed into law the Patient Protection and Affordable Care Act (PL 111-148) (PPACA) on March 23, 2010, as amended by the Health Care and Education Affordability Act of 2010 (HR 4872) (HCEAA) on March 30. Within this legislation, there are drastic changes for both existing and future physician-owned hospitals (POH). The legislation effectively eliminates the "whole hospital" exception to the Stark Laws for new hospitals and provides new restrictions and mandates on existing physician-owned hospitals.

WHAT IS THE WHOLE-HOSPITAL EXCEPTION?

The Stark Law generally prohibits physicians from making referrals for designated health services to an entity with which a referring physician (or an immediate family member) has a financial relationship, unless an exception is met. Penalties for violating the Stark Law include denial of payment and civil monetary penalties ranging from \$15,000 to \$100,000 per violation.

Before passage of PPACA, physicians were generally permitted to refer patients to a hospital in which they had an ownership or investment interest so long as physicians could satisfy the elements of the whole-hospital exception of the Stark Law. Under the Stark regulations that became effective on July 26, 2004, physician hospital ownership was permitted under the following conditions:

1. The referring physician is authorized to perform services at the hospital;
2. Effective for the 18-month period beginning on December 8, 2003 (which expired on May 8, 2005, unless Congress takes further action), the hospital is not a specialty hospital; and
3. The ownership or investment interest is in the entire hospital and not merely in a distinct part or department of the hospital.

This exception is commonly referred to as the whole-hospital exception to the Stark Law. Notably, however, PPACA has significantly narrowed this once broad exception.

HISTORY OF OPPOSITION TO PHYSICIAN-OWNED HOSPITALS

Opponents of physician-owned hospitals, such as Senators Charles Grassley (R-Iowa) and Max Baucus (D-Mont) and Representative Pete Stark (D-Calif), have long argued that physician ownership in hospitals creates

inappropriate incentives for physicians to refer patients. They believe that physician-owned hospitals in which physicians have an ownership interest results in "cherry picking" of the healthiest, wealthiest, and most profitable patients. However, proponents of physician-owned hospitals argue that these facilities provide superior care and stronger clinical outcomes to their patients. As a result of this debate, several attempts have been made to curb or eliminate physicians' ownership and investment in hospitals.

The first significant effort to eliminate physician ownership and investment occurred in the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (MMA), which placed an 18-month moratorium on physician ownership in specialty hospitals and made it a violation of the Stark Law for physicians to refer Medicare patients to any specialty hospital in which a physician had an ownership or investment interest.

Then in 2007, CMS issued a final rule updating the Inpatient Prospective Payment System. Within this rule was a provision requiring all physician-owned hospitals to provide written notice to all patients at the beginning of their hospital stay or outpatient visit that physicians have an ownership or investment interest in the POH. The required notice was intended to promote transparency and to assist patients in making informed decisions regarding care.

Other more recent attempts to prevent construction and expansion of physician-owned hospitals were also made. In January 2009, House Ways and Means Health Subcommittee Chairman Pete Stark inserted a provision into the House's version of the SCHIP bill that would have significantly limited the Stark Law's whole-hospital exception. Also, in March 2009 Senator Grassley proposed introducing a stand-alone physician-ownership ban if such a provision was not included in federal health care reform legislation.

With the passage of the PPACA, all of this history and attempts to quash physician-owned hospitals finally came to fruition.

THE IMPACT OF HEALTH CARE REFORM ON PHYSICIAN-OWNED HOSPITALS

PPACA's amendment to the Stark Law's whole-hospital exception creates significant barriers to new and expanded physician ownership and investment in all hospitals. Molly Sandvig, executive director of the 160-member Physician Hospitals of America, a trade and lobbying organization representing the for-profit, doctor-owned hospitals, said the legislation "destroys over 60 hospitals that are currently under development and leaves little room for the future growth of the industry." Sandvig said the law will put at risk 25,000 jobs in hospitals in 38 states and billions of dollars in investments

PPACA results in the following for physician-owned hospitals:

- Grandfathers licensed physician-owned hospitals that have Medicare provider agreements in place as of December 31, 2010, and that meet certain additional requirements within 18 months of March 23, 2010;
- Establishes a permanent moratorium on the creation or expansion of new physician-owned hospitals after December 31, 2010; and
- Prohibits any aggregate increase of physicians' equity in existing physician-owned hospitals after March 23, 2010

Under the health care reform bill, no new physician-owned hospitals can be built after the close of 2010 and existing physician-owned hospitals will be limited in their expansion and will face heavier regulation and scrutiny.

As of December 31, 2010, the exception to the Stark Law that permitted some physician-owned hospitals will be disallowed and no new physician-owned hospitals will be permitted. Additionally, existing physician-owned hospitals will be grandfathered from this change but will still be precluded from expanding many aspects of the physical facility including beds, procedure rooms, and operating rooms. Finally, the percentage of aggregate physician ownership in existing hospitals cannot be increased after December 31. Any pending or contemplated physician ownership transactions in hospitals will need to be completed by the end of 2010.

LIMITATION ON EXPANSION OF EXISTING PHYSICIAN-OWNED HOSPITALS

After March 23, 2010, existing physician-owned hospitals will be prohibited from expanding the number of beds, operating rooms, or procedure rooms for which they are licensed. Procedure rooms include rooms in which catheterizations, angiographies, and endoscopies are performed, but do not include emergency departments. Physician-owned hospitals must meet specific requirements in order to be allowed to apply to Health and Human Services to add beds, operating rooms, or procedure rooms.

Hospitals may apply for an expansion exception once every 2 years, subject to satisfying a number of stringent criteria that few hospitals will be able to meet. The exception process must allow a period of time for community input regarding the exception application. The exception criteria include: Hospitals applying for the exception must be in a county where population growth is 150% of the population growth of the state in the most recent 5-year period; the applying hospital's annual percent of total inpatient Medicaid admissions must be equal to or greater than the average of such admissions in all hospitals located in the county; the applying hospital must have a bed occupancy rate greater than the state average; the applying hospital must be located in a state where hospital bed capacity is less than the national average bed capacity. Once a hospital meets all of these conditions, it is prohibited from expanding more than 200%.

PROHIBITION ON DEVELOPING NEW PHYSICIAN-OWNED HOSPITALS

In order to meet the whole-hospital exception to Stark regulations, the hospital must have had physician ownership or investment in place and a provider agreement by December 31, 2010. Therefore, the new laws prohibit physician ownership interests in hospitals by the end of 2010.

For physician-owned hospitals currently under construction without a Medicare provider number, they must receive their Medicare provider numbers prior to December 31, 2010, or the hospital will not be allowed to open.

PHYSICIANS CANNOT INCREASE THEIR PERCENTAGE OF OWNERSHIP

The PPACA also caps the total percentage of physicians' direct or indirect ownership or investment interest in a hospital at the percentage owned by all of the physicians in a hospital as of March 23, 2010. The percentage of the total value of the ownership or investment interests held in the hospital by physician owners or investors in the aggregate does not exceed the percentage of ownership/investment interests as of the date of enactment.

Ownership or investment returns must be distributed to each owner/investor in the hospital in an amount that is directly proportional to the ownership/investment interests of the investor.

PATIENT SAFETY GOALS AND CONFLICT OF INTEREST PREVENTION

Existing physician-owned hospitals must submit annual reports containing detailed descriptions of the identity of each physician owner/investor and any other owners/investors in the hospital and the nature and extent of all ownership/investment interests. The hospital must have procedures in place to require that referring physician owners/investors disclose to the patient being referred the ownership or investment interests of the referring physician and any ownership/investment interests of the treating physician. Also, the hospital must now disclose the fact that the hospital is partially owned or invested in by physicians on any public Web site for the hospital and in any public advertising for the hospital.

If a hospital admits patients and does not have a physician available on the premises to provide services during all hours in which the hospital is providing services to patients, **BEFORE** admitting a patient, the hospital **MUST**:

- Disclose this fact to the patient; and
- After the disclosure, the hospital must receive a signed acknowledgement that the patient understands this fact.

The hospital must also have the capacity to provide assessment and initial treatment for patients and refer and transfer patients to hospitals with the capability to treat the needs of the patient involved.

CONCLUSION

In these precarious times of high scrutiny of ownership, in particular physician-owned hospitals, such hospitals must demonstrate their distinction as viable alternatives—integral to the American health care delivery systems. To be successful, it is critical for physicians to distinguish their role in patient care from their role in ownership and governance of the hospital. While it is possible to align these distinctions to achieve optimum patient care, physician owners must at all times adhere to strict federal and state regulatory compliance requirements.

For those physician-owned entities that are in their start-up phases and still under development, the time is now to impress upon regulatory and licensing agencies the urgent need to ensure that necessary licensure and Medicare certification are granted prior to the December 31, 2010, deadline, including receipt of Medicare provider numbers.

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