Tucked into the legislation that would add a prescription drug benefit to Medicare is a provision that would ban physicians from referring patients to specialty hospitals in which they have an ownership or investment interest. Essentially, the change would stop physician investment in or ownership of such hospitals, which is a controversial issue in the hospital industry.

The bill, the Prescription Drug and Medicare Improvement Act, passed the Senate on June 27, 2003. A House-Senate conference committee is meeting to resolve differences between the Senate bill and corresponding legislation passed the same day by the House. The House legislation did not contain the provision barring physician investment in or ownership of specialty hospitals.

The provision specifically bars cardiac, orthopedic, surgical or other specialty hospitals from the so-called “whole hospital exception” of the Stark physician self-referral law, and directs the Secretary of Health and Human Services (HHS) to promulgate a regulation to that effect. The amendment would take effect January 1, 2004. An exception would apply to specialty hospitals that were in operation before June 12, 2003, or that were under development at that date. The Secretary of HHS would determine which specialty hospitals qualify for the exception. The text of the amendment is online at: http://thomas.loc.gov/cgi-bin/query/F?c108:3:./temp/~c108WlhjX0:e796120:

The Congressional action followed a move by the Centers for Medicare and Medicaid Services (CMS) to similarly amend the Stark physician self-referral ban. CMS announced its intention in the semiannual regulatory agenda for HHS, published in the May 27, 2003 Federal Register. CMS later said it would hold off on any regulatory action after objectors complained that it lacked congressional authority to amend the law.

The “whole hospital” exception to the Stark self-referral ban allows physicians to refer patients to hospitals in which they have an ownership or investment interest, as long as that investment is in the entire hospital, not a certain subdivision or department that may more directly benefit from a physician’s referrals. The theory of the original exception was two-fold – physician-owned hospitals then in existence could not readily be banned, and if the services rendered were broad enough, it was unlikely that any one physician-owner could affect a particular hospital. Not so with specialty hospitals. The original statute and regulation recognized the need to avoid the conflicts that arise when a physician owns an interest in hospitals.

While we can’t predict the result of the conference committee deliberations, the leader of the House conference, Rep. Bill Thomas (R-CA), was quoted in The Hill newspaper earlier in 2003 criticizing specialty hospitals as “cash cows” that may strip the profits from local community hospitals by focusing only on the most lucrative procedures.
Specialty continued from previous page

a hospital department or service, but
that conflict is attenuated when the
physician's interest is in the whole
hospital.

The issue of applying the self-referral
ban to specialty hospitals has pitted
general acute care hospitals against
specialty hospitals with physician
owners. The dispute demonstrates
the movement to capture patients
who can afford specialty treatment
outside the general hospital setting.

The dispute also has attracted atten-
tion in Congress for some time. In
April, U.S. Reps. Gerald D. Kleczka
(D-WI) and Pete Stark (D-CA)
introduced the Hospital Investment
Act of 2003 (H.R. 1539), which
would block physicians from owning
or investing in hospital joint ventures
or specialty hospitals on any terms
other than those available to the
general public at the time. The bill
would effectively prevent doctors from
referring patients to hospitals in
which they receive a preferential share
of profits.

In a statement introducing the bill,
Stark decried the rise of specialty
hospitals such as cardiac care or
orthopedic surgery hospitals, stating
that physician investments in such
facilities carry great potential for
conflicts of interest and skirt the
purpose of the self-referral ban that
carries his name. By focusing on
more lucrative procedures, specialty
hospitals “deprive full-scale hospitals
of their most profitable business,
leaving those existing hospitals much
worse off financially,” Stark alleged.

The General Accounting Office
(GAO) issued a report on April 18,
2003 that echoed similar complaints.
The report noted that the number of
specialty hospital facilities has tripled
since 1990, although they still
account for a tiny share of the health
care market (1 percent of Medicare
spending for inpatient services).
About 70 percent of specialty hospi-
tals have some physician ownership,
and slightly more than half are
completely owned by physicians,
according to the report. The report
also alleged that patients at specialty
hospitals tended to be less sick than
patients with the same diagnosis at
general hospitals, appearing to bolster
complaints that physicians with an
ownership interest in a specialty
hospital have an incentive to steer less
sick patients to the specialty hospital,
leaving general hospitals with a sicker,
higher-cost patient population.

The American Surgical Hospital
Association and two major specialty
hospital chains disputed GAO’s
findings and said that physician
ownership of specialty hospitals did
not affect referral behavior. Advocates
of specialty hospitals told GAO that
specialty hospitals can provide high-
quality services more efficiently than
general hospitals because of their
focused mission, and can better tailor
services to patients with a particular
condition. Specialty hospitals also
can allow physicians to treat more
patients than they could in general
hospitals, advocates told GAO.

GAO is preparing a comprehensive
report to be issued later this year on
the effect of specialty hospitals on the
general hospital community.

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Henry C. Fader
To Lead Pepper's
Health Care Practice

Henry C. Fader, a corporate and
health care lawyer, has joined the
firm as a partner and will lead the
firm’s health care practice. Mr.
Fader is a leader in the business
community and serves as first vice
chairman of the board of directors
of the Pennsylvania Chamber of
Business & Industry.

“Henry has earned a reputation as
a ‘go to’ person for difficult busi-
ness issues requiring clear thinking
and diplomatic resolution,” said
David W. Sweet, a partner in
Pepper’s Harrisburg office and vice
chairman of the firm’s Executive
Committee. “He was tapped to
help with Governor Rendell’s
Health Care Task Force and with
matters involving The Barnes
Foundation, and he is an effective
and well-regarded leader of the
Pennsylvania Chamber of Business
& Industry.”

“Henry is a senior corporate lawyer
with a significant reputation in the
health care legal field,” added
Robert E. Heideck, Pepper’s
executive partner. “His interest in
technological evolution and his
experience in telemedicine, elec-
tronic medical records and HIPAA
complement our multidisciplinary
health care practice. We are happy
to welcome him to the firm.”

Before joining Pepper, Mr. Fader
was a partner and chairman of the

See Fader on next page
Mr. Fader’s corporate and health care practice includes acquisitions, mergers and other transactions, organizational structuring, operational issues, succession planning and intergenerational transfers of closely held businesses. He has particular experience in matters involving e-commerce and Internet businesses. In health care, he has formed integrated delivery systems and advised on tax-exempt financing, the formation and governance of nonprofit organizations, corporate governance of health care institutions and regulatory issues.

Pepper is developing its health care practice to emphasize technology and the innovations it brings to the health care industry. Mr. Fader is particularly experienced in this area. He counsels clients on the implementation of telemedical solutions and computerized patient records, and on compliance with the privacy and security requirements of the Health Insurance Portability and Accountability Act (HIPAA) and state laws relating to privacy.

Mr. Fader is active in many professional and civic organizations. In addition to his leadership role with the Pennsylvania Chamber of Business & Industry, he is chairman of the board of directors of Intercultural Family Services, Inc., and solicitor and a board member of Eagleville Hospital. He is a former president and board member of the e-Pennsylvania Alliance and a former chairman of the Pennsylvania Information Highway Consortium Task Force on Telemedicine. Mr. Fader is active in the American Health Lawyers Association, the National Association of Bond Lawyers and the Healthcare Financial Management Association. He is a frequent writer and speaker.

Mr. Fader is a graduate of the University of Rochester (A.B. 1968) and Syracuse University College of Law (J.D. 1973). He is admitted to practice in Pennsylvania and New Jersey.

Joining Mr. Fader at Pepper will be Rebekah A.Z. Monson, formerly an associate with Schnader Harrison Segal & Lewis. Ms. Monson’s practice concentrates on providing corporate legal counsel and transactional advice to health care providers and others. She has experience in preemption issues in Pennsylvania involving HIPAA, telemedicine and Internet applications for health care organizations. Ms. Monson has experience in general corporate law and capital financing, including municipal and tax-exempt financing.

Ms. Monson is a graduate of Georgetown University Law Center (J.D. 1998), Barnard College (B.A. 1995) and the Jewish Theological Seminary of America (B.A. 1995).

Pepper in Public

A Roundup of Recent and Upcoming Activities by Pepper Health Care Lawyers

**Articles**

Pepper lawyers write frequently about issues of interest to the health care community. All the articles below are available on Pepper’s Web site, www.pepperlaw.com:


“Pa. Malpractice Reforms Could Set the Pace for Other States,” by Andrew R. Rogoff and Imiebihoro T. Ahonkhai, Physician Executive, May/June 2003


**Upcoming Events**

in Philadelphia. For more information visit our Web site.


“Hedge Funds and Advisers: Life Cycle Issues,” September 17 and October 7, 2003. These are the last two sessions of a five-part series of breakfast briefings by Gregory J. Nowak. All sessions are at the Philadelphia Country Club. For more information or to register, contact Nellie Spencer (215.981.4905; spencern@pepperlaw.com) or visit our Web site.

Recent Events

Barry H. Boise conducted two breakout sessions at the 12th Annual National Expert Witness and Litigation Seminar on June 26-27. His sessions were on “Pleasing the Client: What Attorneys Are Really Looking for From Experts,” and “Acting as an Expert Consultant.”

John W. Jones Jr. spoke about HIPAA privacy and security issues at a seminar in Reading, Pa., on June 25. The event was sponsored by Lorman Education Services.

Feedback Wanted

What health care issues keep you up at night? Drop us a line and let us know, and we'll write about it in an upcoming issue of Health Care Law Alert. Contact Henry C. Fader, 215.981.4640 or faderh@pepperlaw.com.