



Client Alert



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Healthcare Reform’s New Restrictions on “Whole-Hospital Exception” — Changing Regulatory Landscape for Physician-Owned Hospitals

As we reported in an earlier article [S. Welch and J. Blakely, “Significant Healthcare Reform Provisions that Impact Physicians,” May 12, 2010],¹ Section 6001 of the Patient Protection and Affordable Care Act (PPACA) imposes extensive restrictions on the Physician-Self Referral Law’s (Stark Law) “whole-hospital exception” and effectively bars future physician investment in specialty hospitals.

According to Physician Hospitals of America (PHA), Section 6001 has already halted the development of 39 physician-owned hospitals.² Additionally, 45 hospitals currently under development are at risk of failing to meet Section 6001’s strict compliance requirements.³ PHA is attempting to prevent enforcement of Section 6001 by filing a joint suit with a 20-bed private Texas hospital challenging the constitutionality of the law. This article outlines the provisions of Section 6001 and analyzes the recent legal challenge.

New Requirements Under Section 6001

As our earlier article noted, Section 6001 significantly restricts application of the Stark Law’s whole-hospital exception. The Stark Law generally prohibits a physician who has a financial relationship with an entity from making referrals to that entity for services payable by Medicare.⁴ However, the Stark Law provides an exception if the physician has an ownership or investment interest in the hospital’s entire business—the whole-hospital exception.

Under Section 6001, the whole-hospital exception will apply only to “grandfathered” hospitals – i.e. existing hospitals that have existing physician investment and existing provider agreements with CMS by December 31, 2010. Exempted hospitals cannot increase physician ownership percentages as of March 23, 2010. The PPACA further restricts the whole-hospital exception by placing additional requirements on these hospitals, including:

1 http://www.agg.com/media/interior/publications/Welch_Blakely-Significant_HC_Reform_Provisions_Impact_Physicians.pdf
2 Press release, Physician Hospitals of America, “Federal Lawsuit and Injunction Filed Challenging Limitations on Physician Owned Hospitals in Healthcare Reform” (June 3, 2010), available at http://www.physicianhospitals.org/physician_press_release.php.
3 *Id.*
4 42 U.S.C. § 1395nn(a)(1)(A) (2009).

1. *Preventing Conflicts of Interest*

To prevent conflicts of interest, the PPACA requires the following:

- Hospitals must submit an annual report to HHS disclosing the identity of each physician owner and the nature and extent of their interest.
- Referring physicians or investors must disclose any interest in the hospital or treating physician to the referred patient in time for the patient to make a meaningful decision regarding the receipt of care.
- Hospitals may not limit physician ownership or investment to those making or influencing referrals.
- Public websites and advertising must disclose the fact that the hospital is partially owned or invested in by physicians.

2. *Ensuring Bona Fide Investments*

The PPACA attempts to ensure investments in physician-owned hospitals are made in good faith by mandating the following:

- The percentage of total value of the ownership or investment interests held in the hospital by physicians in the aggregate may not increase.
- Hospitals may not offer physician owners or investors more favorable terms of ownership than those offered to non-physician owners.
- Hospitals or any owner or investor in a hospital may not provide loans or financing, guarantee a loan, make a payment toward a loan, or otherwise subsidize a loan to any physician owner or investor.
- Ownership or investment returns must be distributed to investors in an amount that is directly proportional to the investment or ownership by the hospital investor.
- Physician owners and investors may not receive any guaranteed receipt of or right to purchase other business-related interests in the hospital.
- Hospitals may not offer any physician owner or investor the opportunity to purchase or lease any property under the control of the hospital on more favorable terms than the terms offered to an individual who is not a physician owner or investor.

3. *Improving Patient Safety*

The PPACA attempts to improve patient safety by requiring the following:

- Hospitals must have the capacity to provide assessment and initial treatment for medical emergencies.
- Hospitals must have procedures in place to facilitate the referral and transfer of patients to hospitals with the required capability to treat the needs of the patient involved.
- If the hospital does not have a physician available on premises during all hours in which the hospital is providing services to a patient, the hospital must disclose such fact to the patient and receive a signed acknowledgment from the patient. all hospitals located in the county.

4. *Limiting Expansion*

Under the PPACA, physician-owned hospitals are generally prohibited from expanding. However, certain hospitals may qualify for an expansion exception in limited circumstances. To qualify, five requirements must be met:

- The hospital must be located in a county that has had an increase in population during the prior five-years of at least 150 percent of the population increase in the state.
- The annual percent of total Medicaid inpatient admissions for the hospital must be equal to or greater than the average percent of such admissions for all hospitals located in the county.
- The hospital must not discriminate against beneficiaries of federal healthcare programs, nor permit physicians practicing at the hospital to discriminate against such beneficiaries.
- The hospital must be located in a state in which the average bed capacity in the state is less than the national average bed capacity.
- The hospital must have an average bed occupancy rate that is greater than the average bed occupancy rate in the state.

If a hospital qualifies under the above requirements, the PPACA further restricts eligibility to one exception every two years. Additionally, expansion is capped at 200 percent, and any expansion must occur in facilities on the hospital's main campus.

Legal Challenge to Section 6001

PHA, a trade group for physician-owned hospitals, and Texas Spine & Joint Hospital (TSJH) jointly filed suit on June 3, 2010, challenging the constitutionality of Section 6001.⁵ In their complaint, PHA and TSJH claim that Section 6001 violates their due process and equal protection rights and that the Section is void due to its contradictory, vague and arbitrary nature. Specifically, they claim that Congress's purpose in enacting Section 6001 is illegitimate, because it aims "to constrict the economic effectiveness of physician-owned hospitals to benefit non-physician-owned hospitals." Furthermore, the complaint alleges that Section 6001 is unconstitutionally vague. Generally, a statute may be void for vagueness if it fails to give adequate notice to the public of prohibited behavior or adequate guidance to law enforcement in prosecuting violations. PHA and TSJH claim that Section 6001 imposes unclear and contradictory limitations on physician-owned hospitals' right to expand, making it unconstitutionally vague. Finally, the complaint alleges that enforcement of Section 6001 constitutes an unconstitutional taking without just compensation, because TSJH has spent nearly \$3 million in preparation of an expansion that they claim will be lost if this Section is enforced. On those grounds, TSJH seeks an injunction to prevent enforcement of Section 6001 and to allow TSJH to move forward with their planned expansion.

The outcome and timeline of this case are uncertain. However, the litigation will play an important role in determining the impact of Section 6001 on physician-owned hospitals.

⁵ Complaint for Declaratory and Injunctive Relief, *Physician Hosps. of Am. v. Sebelius*, No. 6:10-cv-00277 (E.D. Tex. filed June 3, 2010), 2010 WL 2243159.

Conclusion

Section 6001 of the PPACA significantly impacts existing physician-owned hospitals and the potential for development of new physician-owned hospitals. Many existing physician-owned hospitals will need to restructure several aspects of their practices and procedures to comply with the Act. These changes may include revising organizational documents, policies, admissions forms and websites. It is unclear whether PHA and TSJH will be successful in their attempt to prevent Section 6001 from being enforced. Thus, physician-owned hospitals should pay close attention to the requirements of Section 6001 and the developments of the legal challenges as they attempt to move forward under the PPACA.

Ms. Rubinger and Ms. Cohen would like to thank Christina Weatherford who assisted significantly with the preparation of this article. Ms. Weatherford is a current law student and a summer associate of Arnall Golden Gregory LLP. Ms. Weatherford is not yet admitted to the State Bar of Georgia.

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