



Impact of Physician-owned Limited-service Hospitals: Oklahoma City Case Study

February 16, 2005

*Based on a case study of market dynamics and
community impacts completed by McManis
Consulting between October and December 2004.*

Executive Summary

- **Seven new physician-owned limited-service hospitals opened between 1994 and 2005 in a competitive market including:***
 - 10 full-service hospitals representing several major systems.
 - 26 ambulatory surgery centers (including over 1,300 physician ownership positions).
- **Physician-owners quickly re-directed patients with favorable reimbursement to the new facilities.**
- **The full-service hospitals have had to reduce services to compensate for lost patients and revenues.**
- **Many physician-owners reduced or eliminated their emergency call obligations, bringing the only Level I trauma center in the state to the brink of closure.**
 - To avert a crisis, a system of rotating coverage was negotiated among physicians and seven full-service hospitals.
 - Specialists continuing to accept emergency call (particularly at inner city hospitals) bore an increased burden. The higher load of emergency cases was “crowding out” better reimbursed elective cases, resulting in reduced physician incomes, higher stress, and difficulty in recruiting new physicians.

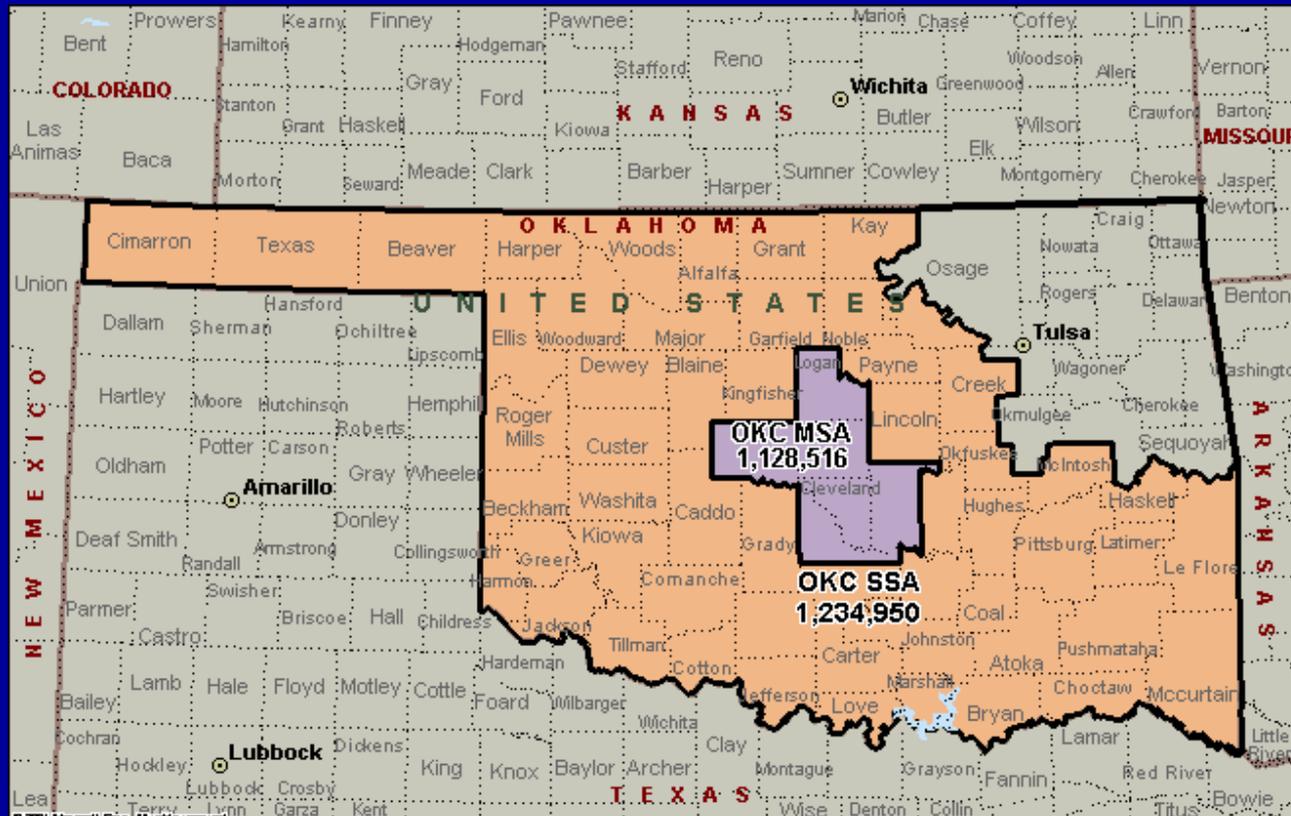
* Six of the new limited-service hospitals were physician-owned, some with participation by private investors. Two included local hospital systems as investors. An eighth hospital was scheduled to open in 2005.

Executive Summary (continued)

- **The limited-service hospitals selected patients who could generate high profits, focusing on:**
 - the best paid procedures (cardiac care, spine surgery, general surgery and gynecological surgery)
 - elective (non-emergency) procedures
 - patients insured by acceptable payers (commercial plans and Medicare for some services)
- **These practices yielded high profits and lifestyle improvements for physician owners.**
 - The Oklahoma Spine Hospital generated margins in excess of 40%, and annual profits of approximately \$700,000 per physician-owner.
 - The absence of emergency cases helped physician-owners gain much greater control over their personal schedules.
- **The remaining patients continued to be treated in the community hospitals.**
 - Full-service hospitals declined financially as a result of the diversion of their best reimbursed services.
 - Operating costs also increased.
 - This led to cutbacks in other less well-reimbursed services.

Introduction

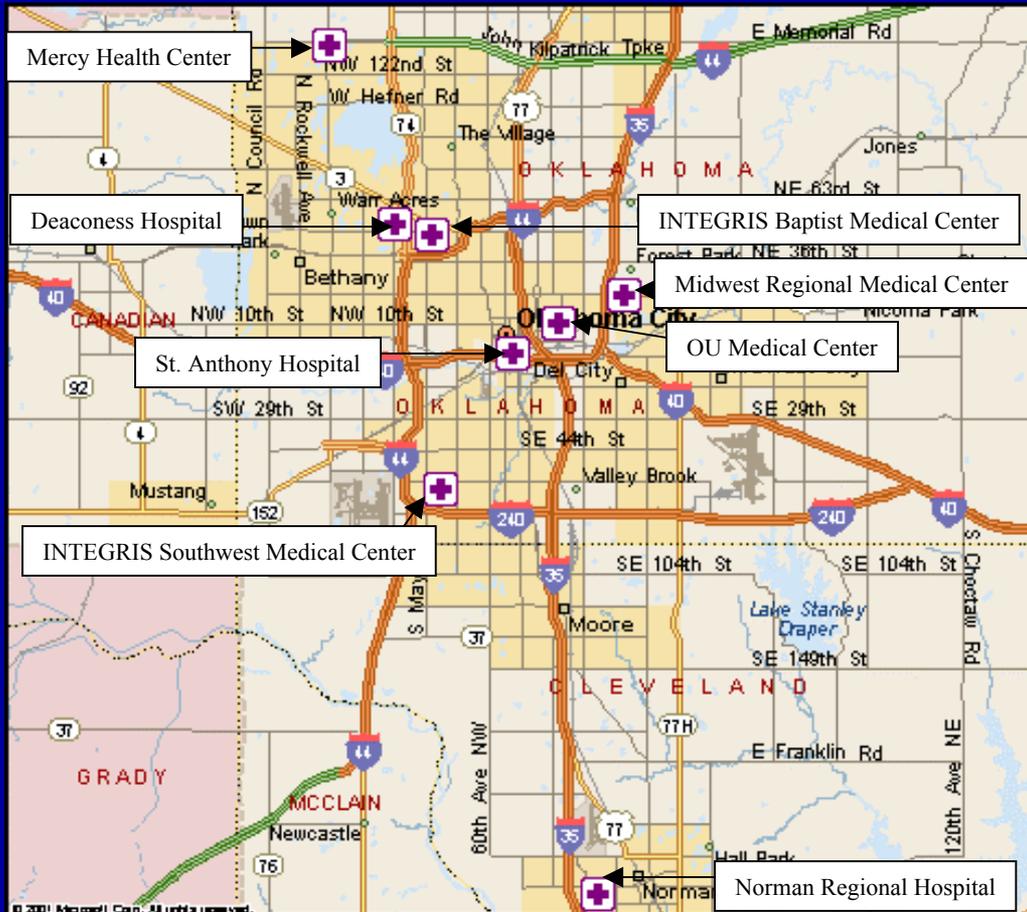
The hospitals in Oklahoma City serve the metropolitan area and (together with those in Tulsa) provide most of the tertiary care for the state.



The Oklahoma City metropolitan area has a population of 1.1 million.

Area hospitals also provide care to a predominantly rural secondary service area with a population of 1.2 million.

Oklahoma City's hospital market is highly competitive with 10 general acute-care hospitals, representing several major hospital systems.*



- **University of Oklahoma (OU) Medical Center** – 3 hospitals in separate towers, the regional trauma center and primary safety net hospital, partially owned by HCA (727 beds)
- **INTEGRIS Baptist Medical Center** (469 beds) and **INTEGRIS Southwest Medical Center** (351 beds) - part of a statewide not-for-profit system
- **Mercy Health Center** – a suburban tertiary center, part of the Sisters of Mercy of St. Louis system (416 beds)
- **St. Anthony Hospital** – located in downtown OKC, part of the SSM of Oklahoma system (428 beds)
- **Deaconess Hospital** – a full-service not-for-profit hospital (313 beds)
- **Norman Regional Hospital** – an independent hospital serving the college community (297 beds)
- **Midwest Regional Medical Center** – an independent hospital in southeast OKC (247 beds)

* HCA also owns nearby Edmond Medical Center, and INTEGRIS includes Canadian Valley Regional Hospital (not shown on map).

Oklahoma City has long been a focus of physician entrepreneurial activity.

- **There were 26 physician-owned ambulatory surgery centers in OKC as of mid-2004:**
 - 14 multi-specialty centers
 - 7 orthopedic centers
 - 3 gastroenterology centers
 - 1 ophthalmology center
 - 1 plastic surgery center
- **Together, these centers represented over 1,300 physician-ownership interests.**
 - Some physicians had interests in more than one center.
 - Several corporations (including HEALTHSOUTH, U.S. Surgical, Integrated Medical Delivery and Symbion) also had interests.

Source: McManis Consulting, assembled from multiple sources.

Seven new physician-owned limited-service hospitals opened in Oklahoma City between 1994 and 2005.

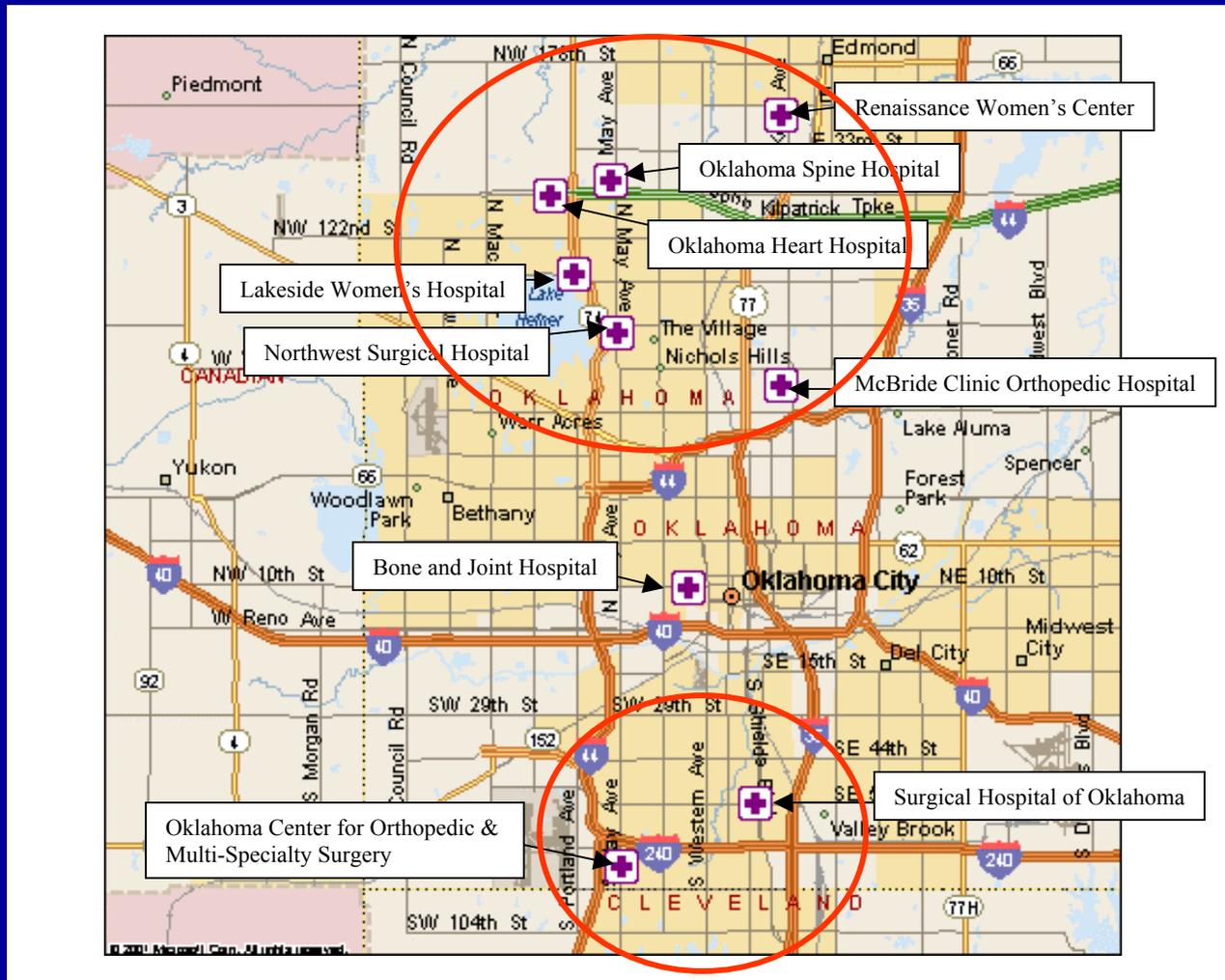
One existing not-for-profit limited-service hospital

- **Bone & Joint Hospital** (102 beds; not-for-profit; started in 1920s; part of the SSM of Oklahoma system that owns St. Anthony)

was joined by these physician-owned limited-service hospitals ...

- **Northwest Surgical Hospital** (opened 1994; orthopedics focus; 9 beds)
- **Lakeside Women's Hospital** (33 beds; physician-owned; started in mid-1990s)
- **Surgical Hospital of Oklahoma** (established by physicians and HealthSouth in 1996, 100% physician-owned since 2003, 12 beds)
- **Renaissance Women's Center** (opened 1997, 80% physician-owned, 20% owned by INTEGRIS, 14 beds, 19 bassinets)
- **Oklahoma Spine Hospital** (opened 1999; 18 beds; owned by 15 neurosurgeons)
- **Oklahoma Heart Hospital** (opened in 2002, 78 beds; 49% physician-owned; Mercy Health System owns 51%)
- **Oklahoma Center for Orthopedic & Multi-Specialty Surgery** (opened 2002)
- **McBride Clinic Orthopedic Hospital** (opening in 2005; 40 beds); this group has traditionally practiced at the Bone & Joint Hospital.

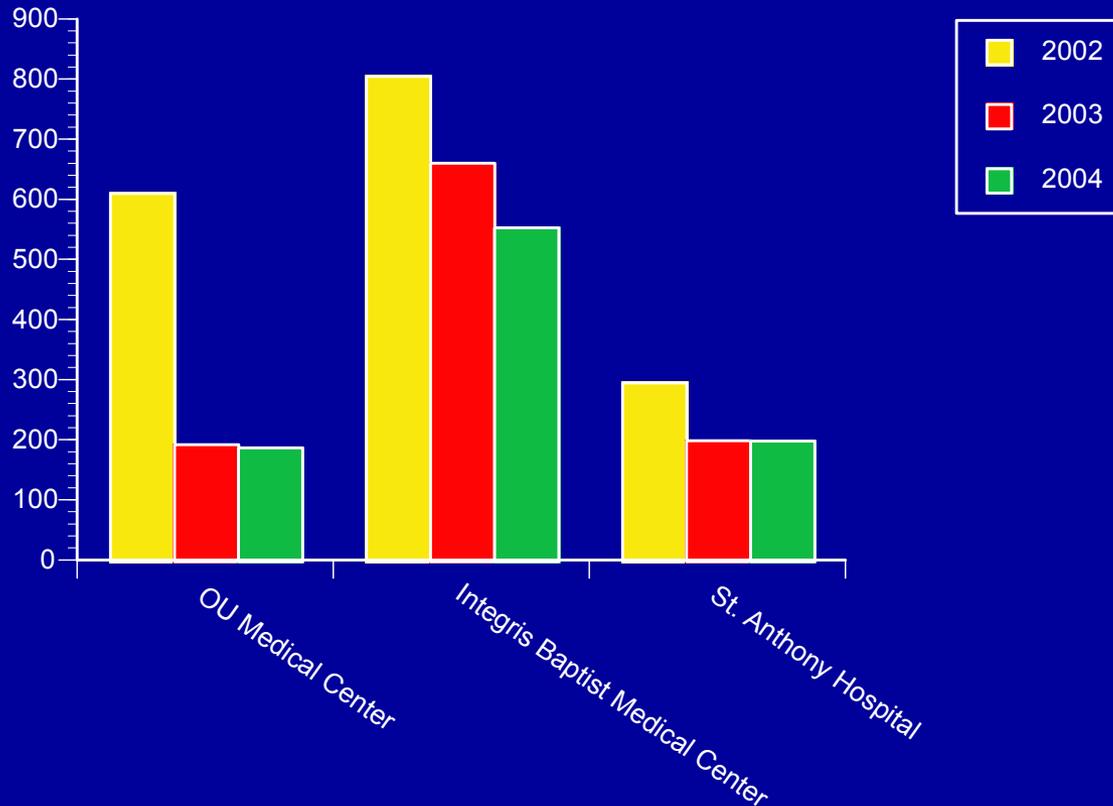
The new limited-service hospitals are located in Oklahoma City's two high-income growth corridors (to the northwest and the south).



Patient Selection

Physicians quickly shifted their patients to limited-service hospitals in which they had an ownership position.

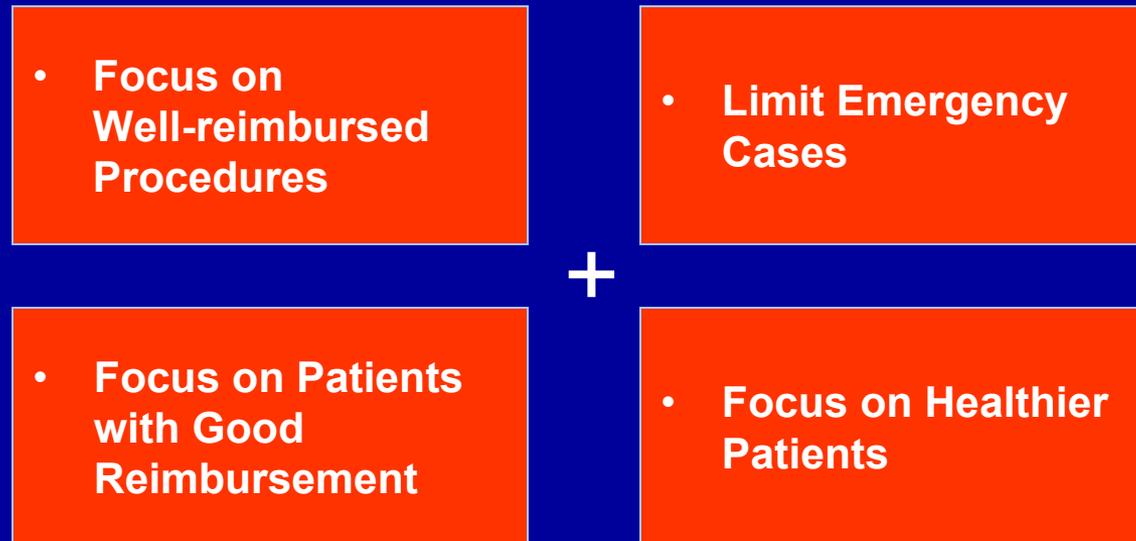
Reductions in the Number of Coronary Bypass Surgeries at Three Full-service Hospitals after the Oklahoma Heart Hospital Opened in August of 2002



Source: OUMC, INTEGRIS and St. Anthony's administrations. Oklahoma Cardiac Associates (OCA) practiced at these three hospitals, at Deaconess Hospital, and at Mercy Health Center prior to their establishment of the heart hospital as a partnership with Mercy.

Patient selection helped to create significant profits and high physician-owner satisfaction in the limited-service hospitals.

Patient selection by physician-owned limited-service hospitals



- resulted in -

High profits for limited-service hospitals and their investors, and high physician-owner satisfaction

- but also -

Reduced resources available to meet the community's broader health care needs

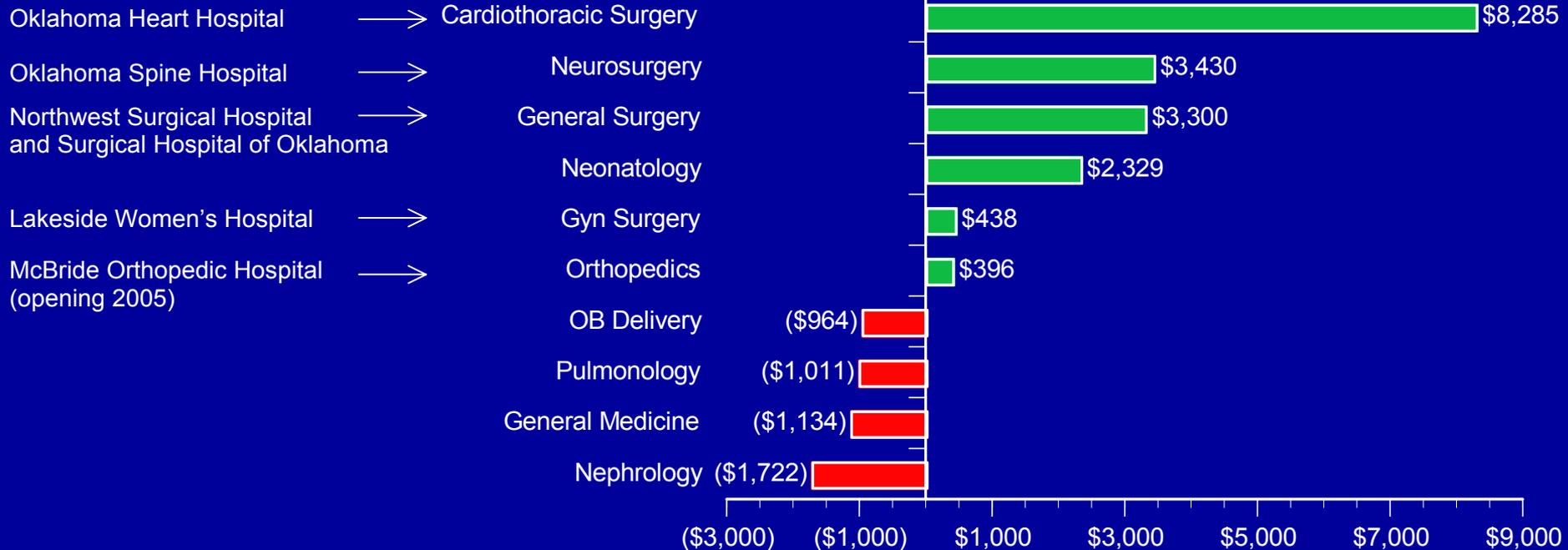
Why do these patient selection tactics yield high profits?

- **Certain services and patients are more well-paid than others:**
 - Procedure-based services -- cardiovascular care, spine surgery, orthopedics, general surgery -- tend to pay more relative to costs than medicine, obstetrics, and behavioral health.
 - Private payers pay more relative to costs than Medicare and Medicaid.
 - The standby capacity for emergency services is costly to maintain and is under-reimbursed.
 - Fixed payment systems don't reimburse more for sicker patients, except for "outliers".

The physician-owned limited-service hospitals were organized to focus on well-paid procedures in Oklahoma City.

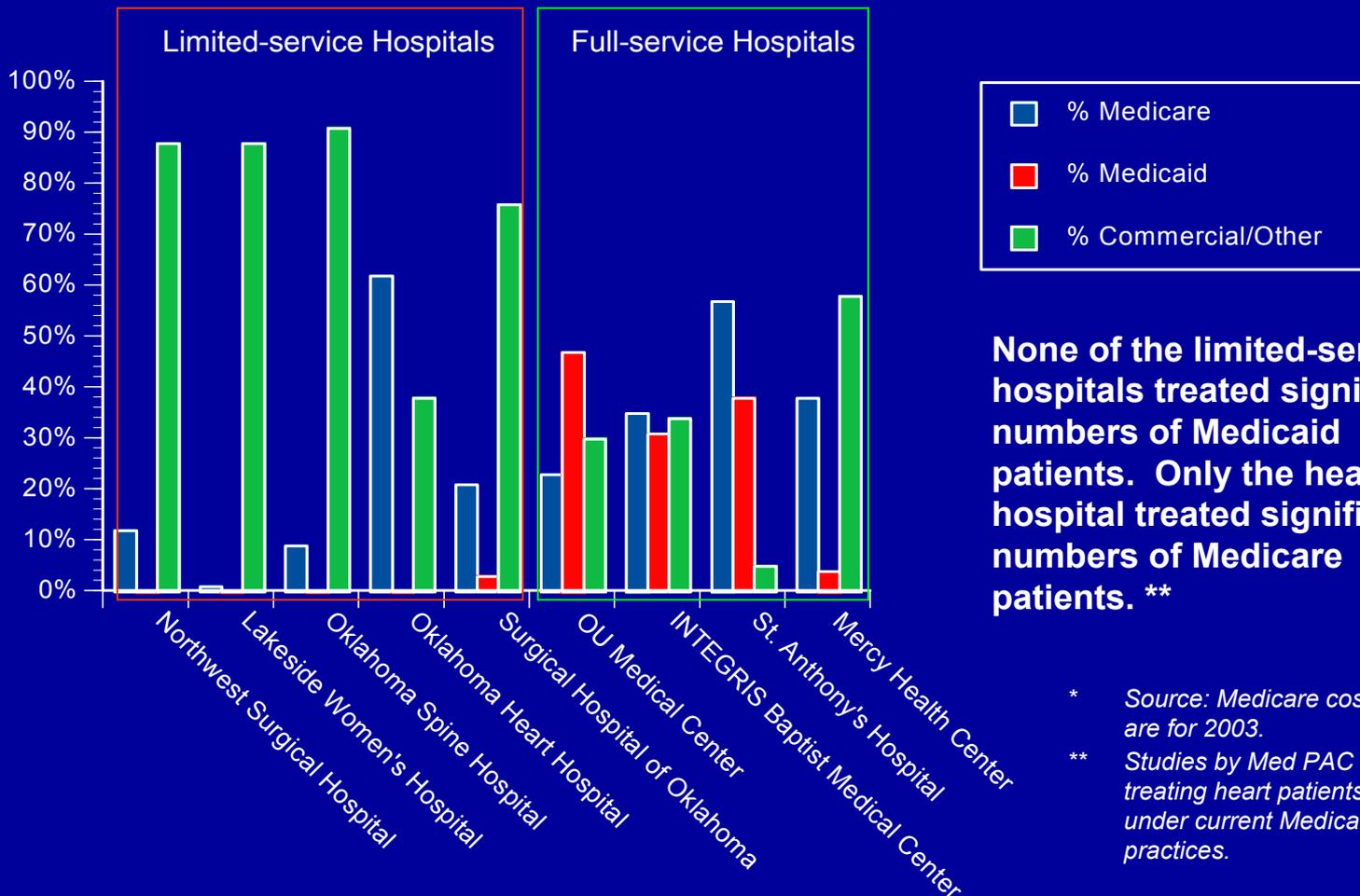
Major Limited-service Hospitals, Arrayed by Targeted Cases

Net Income per Case, Selected Diagnostic Groupings, INTEGRIS, 2003



The limited-service hospitals avoided poorly reimbursed Medicaid patients.

Payer Mix of Major Limited and Full-Service Hospitals *



None of the limited-service hospitals treated significant numbers of Medicaid patients. Only the heart hospital treated significant numbers of Medicare patients. **

* Source: Medicare cost reports. Data are for 2003.
 ** Studies by Med PAC have found that treating heart patients is profitable under current Medicare reimbursement practices.

The current limited-service hospitals offer minimal emergency services.

Consistent with Oklahoma law, all of the limited-service hospitals have emergency rooms; however most are limited to small spaces, have limited signage, and treat very few patients. *

Avoiding emergency cases helps to maximize profits and create physician-owner satisfaction. Managers are able to:

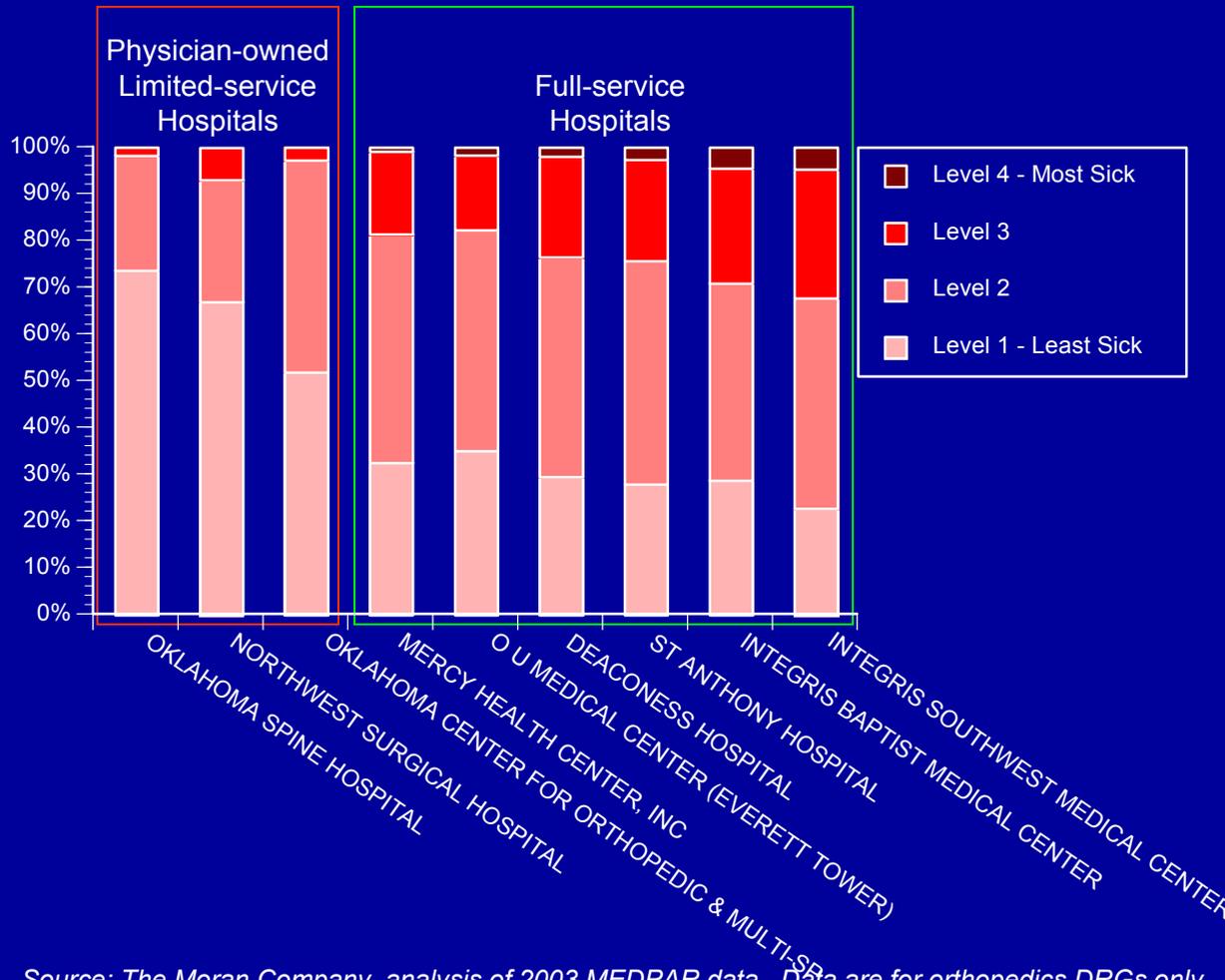
- Avoid purchases of seldom-used equipment
- Plan in advance without the potential for emergency cases to disrupt the schedule
 - Match staffing to cases, avoiding the costs of standby capacity
 - Offer an attractive schedule for physicians (free of interruptions)
 - Provide physicians with a practice environment without the responsibilities of night and weekend call
- Exert control over acuity and payer mix (avoiding EMTALA mandate) **

* *The Oklahoma Heart Hospital, which is 50% owned by Mercy Health Center, offers full emergency services, and the McBride Orthopedic Hospital, scheduled to open in 2005, has announced it will have an orthopedic emergency service.*

** *The Emergency Medical Treatment and Labor Act (EMTALA) requires hospitals with emergency departments to screen and stabilize all patients, regardless of ability to pay.*

Physician-owned limited-service hospitals treated less acutely ill patients than did the full-service hospitals.

APR-DRG Case Mix (Orthopedics Cases)



Physician-owned limited-service hospitals treated orthopedic patients in Levels 1 and 2 almost exclusively, while the full-service hospitals treated a mix.

The same trend was noted in general surgery cases.

In cardiac cases, the Oklahoma Heart Hospital also had the least acute case mix.

Source: The Moran Company, analysis of 2003 MEDPAR data. Data are for orthopedics DRGs only.

Impacts on the Health Care Delivery System

The introduction of so many physician-owned facilities had several impacts on the OKC health care delivery system. *

A positive impact for selected groups ...

- Excellent financial returns for limited-service hospitals and their owners
- Enhanced “quality of practice” for many physician-owners
- Increased competition for staff with skills sought by the limited-service hospitals, leading to bonuses and salary increases

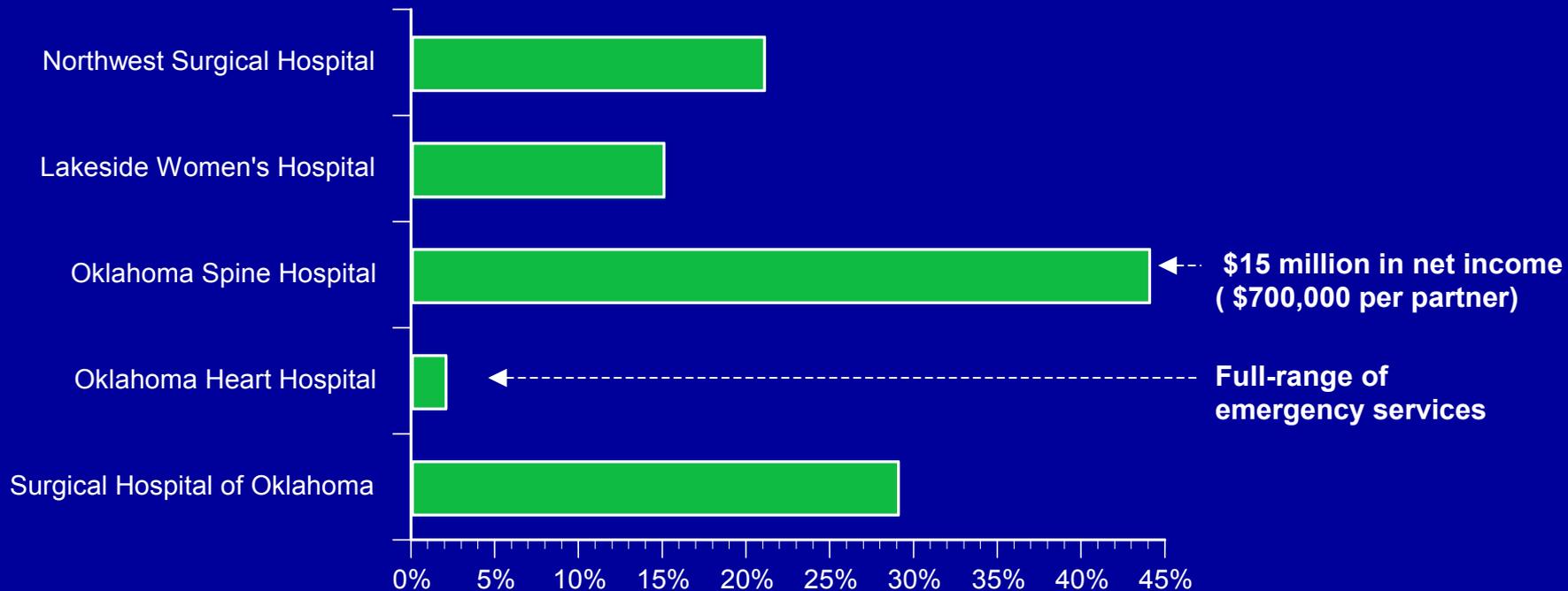
... and a negative impact on the broader community

- Threats to financial survival for some full-service hospitals
- Deteriorating “quality of practice” for physicians continuing to take emergency call at full-service hospitals
- A crisis in trauma service
- Growing difficulties in operating inner city emergency services
- Terminations of programs and staff in less profitable health services

* Consistent quality of care and patient service data were not available. The Oklahoma Heart Hospital had documented excellent quality and service performance, as had INTEGRIS Baptist's heart program. The Oklahoma Spine Hospital had good outcomes as reported by HealthGrades.com.

The physician-owned hospitals generated high profits for investors ...

Profit Margins of Major Physician-owned Limited-service Hospitals, 2003



Source: Medicare cost reports. Margins reported here are Net Income / Net Patient Revenue. In addition to a full-range of emergency services, the Oklahoma Heart Hospital treats significant numbers of Medicare patients and has a not-for-profit hospital partner.

... meanwhile, the full-service hospitals experienced financial downturns, and some were in serious financial distress.

- **Hit hard by the specialty hospitals, OU Medical Center secured \$5.7 million annually in relief from the state to subsidize its Level I trauma service (only Level I trauma center in state).**
- **Deaconess Hospital entered discussions with potential purchasers/merger partners.**
- **Already hurt by the opening of the heart and surgical hospitals, St. Anthony was now threatened by the opening of the McBride Orthopedic Hospital. Their affiliated Bone & Joint Hospital, the historical partner of the McBride Clinic, was generating more net income (\$5 million per year) than the much larger St. Anthony's.**

"The State of Oklahoma had to increase our Medicaid rates by \$5.7 million a year for us to continue to operate our Level I trauma service. If we hadn't lost the income from cardiac services, we wouldn't have needed this State money. So, the taxpayers are paying extra."

Chief Financial Officer, OU Medical Center

Physician-owners of limited-service hospitals were enjoying better “practice lifestyles” ...

- **Most physician-owners either sharply reduced or totally eliminated their emergency call obligations (emergency room and trauma coverage). ***
- **Without these responsibilities, physicians found their practice lifestyles more predictable and less stressful.**

“I love being able to control my schedule. Between surgeries I can have a cup of coffee, dictate notes and call my office, and when I walk in to see the second patient, everything is ready to go.”

Organizer and shareholder of Oklahoma Spine Hospital

* Physician-owners of the spine and heart hospitals limited their call obligation to nearby Mercy Health Center. Others were able to avoid call obligations at any hospital.

... but reductions in emergency call coverage by physician-owners of limited-service hospitals helped precipitate a statewide crisis in trauma coverage.

- **Before the crisis, several Oklahoma City hospitals provided Level II trauma coverage and OUMC provided the Level I trauma coverage for the state.**
- **When the neurosurgeons and other critical specialists opted out of call coverage, the Level II trauma hospitals could no longer meet state standards for specialty coverage.** They began to downgrade to Level III status.
- **This placed unsustainable burdens on OUMC, which threatened to drop its Level I coverage** unless others reinstated Level II coverage.
- **In the face of public pressure, the county medical society, the state hospital association and others brokered a compromise ...**
 - Neurosurgeons and other critical sub-specialists who had dropped off call agreed to provide coverage for one Oklahoma City hospital each night to allow for a rotating Level II trauma service.
 - Meanwhile, OUMC and the university physicians would continue to provide Level I coverage.
 - Thus far, the voluntary compromise has held up. Most physicians in the critical sub-specialties are participating.

The withdrawal of specialists from call coverage placed a greater burden on physicians at inner-city hospitals with busy emergency rooms.

- **Many physician owners reduced their admissions at the acute-care hospitals below the levels where they were required to participate in call coverage.**
- **This increased the call coverage obligations for remaining surgeons, which**
 - Increased emergency time commitments and stress for the remaining surgeons.
 - Reduced their earnings potential. **Emergency patients bring poor reimbursement in most sub-specialties. As emergency cases “crowd out” elective cases on a physician’s schedule, physician income falls.**
- **This has caused additional surgeons to leave these hospitals, and has made it extremely difficult to recruit replacements.**

“They take the elective cases, but not the emergencies ... then the rest of us have our calendars filled with emergencies. Many of us can’t make a living that way.”

General Surgeon, INTEGRIS Southwest Medical Center

The concentration of emergency cases at the full-service hospitals has led to staff dissatisfaction.

- “A surgery isn’t just a surgery. By having fewer elective surgeries and more emergency surgeries, our nurses are terribly stressed.”
- “Saints is definitely doing more complex cases, and the patients are sicker. Less complex cases are done at the surgery centers and specialty hospitals.”
- “St. Anthony’s handles four or five add-ons (unscheduled surgeries) a day, including a number from physicians who are busy doing surgery at their own ASCs and specialty hospitals during the day.”

Nurse managers at St. Anthony Hospital

Competition for staff increased labor costs – higher salaries, bonuses and turnover costs.

Staff Turnover and Inducements to Avoid Turnover at OU Medical Center

	Lost Staff	Cost of Turnover
Registered Nurses	40	\$ 1,664,000
Respiratory Therapists	3	\$ 41,600
Other	13	\$ 459,680
Subtotal	<u>56</u>	<u>\$ 2,165,280</u>
Bonuses to Prevent ICU Closure		\$ 466,000
Total		<u><u>\$ 2,631,280</u></u>

Source: OU Medical Center administration.

... but cost-cutting measures eliminated positions and some programs in under-reimbursed services

**St. Anthony's Response to
Financial Losses Associated with
Limited-service Hospitals**

- Closed outpatient clinics around the city
- Reduced the medical education program
- Reduced the eye surgery program
- Closed the child behavioral day treatment program

Source: St. Anthony's administration.

Summary

- **Seven new physician-owned limited-service hospitals were added in a 10-year period to an already highly competitive market**
- **Physician-owners were successful in:**
 - Re-directing selected patients to their facilities
 - Selecting the most profitable patients and providing them with attractive treatment experiences
 - Realizing excellent financial returns
 - Improving “practice lifestyles” by reducing their emergency call obligations and focusing on elective cases
- **Impacts were negative for non-participating hospitals and physicians, their staff and the community as a whole:**
 - Helped precipitate a state-wide crisis in trauma coverage
 - Created staff stress and dissatisfaction at full-service hospitals with the growing focus on emergency cases
 - Increased financial and lifestyle burdens for those surgeons who continue to take emergency calls
 - Forced cutbacks and closures in poorly reimbursed services



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