Hooper Lundy & Bookman, Inc.

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Terminated Physicians May Be Entitled to Fair Procedure, Supreme Court Rules

In a 4-3 decision, the California Supreme Court has ruled that under specific circumstances physicians are entitled to fair procedure before they can be terminated from an insurer's preferred provider list.

The closely watched case, *Potvin v. Metropolitan Life Insurance,* was brought by a physician who was given notice by an insurer that he would no longer be listed as one of its preferred providers. The insurer provided no reason for the physician's removal. The physician subsequently requested a reason and a hearing. The insurer terminated its relationship with the physician pursuant to the provisions of its contract, which permitted either party to terminate on 30 days notice, without cause.

The physician argued that he was entitled to the same type of "fair procedure" that would be granted if he were to lose hospital privileges. The insurer refused to provide a hearing, but ultimately informed the physician that he was terminated because he no longer met the insurer's criteria, which required that physicians have less than two malpractice claims against them. The plaintiff physician had had four such claims filed against him.

In its ruling, the Supreme Court held that physicians are entitled to fair procedure before they can be terminated from an insurer's preferred provider list, but only if the insurer is found to possess "power so substantial that the removal significantly impairs the ability of the ordinary, competent physician to practice medicine or a medical specialty in a particular geographical area, thereby affecting an important, substantial economic interest." The Court held that the "without cause" termination clause was unenforceable to the extent that it purported to limit the right to fair procedure, where that right applied.

The Court also stated that "our holding . . . does not prevent an insurer, subject to obligations of common law fair procedure, from exercising its sound business judgment when establishing standards for removal of physicians from its preferred provider lists. We simply hold that, under principles recognized by the common law of this state for over a century, such removal must be 'both substantively rational and procedurally fair' . . ."

"Even when this common law right does apply, an insurer may remove a physician from its preferred provider list without regard to the financial effect on the physician, so long as the insurer's decision is 'substantially rational and procedurally fair.'"

The Court expressly noted that this opinion does not apply to employer-employee relationships.

The dissenting opinion essentially argues that the Court is unfairly protecting the income of physicians while

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it does not do so for others, and is purporting to find "public policy" protecting such contract relationships where there has been no articulation of such public policy by the legislature. It also argues that the standard announced by the majority is unworkable, since it will require a case-by-case analysis to determine whether the particular insurer has sufficient power in a particular geographic area to significantly impair the ability of an ordinary, competent physician to practice medicine or a medical specialty in that geographic area.

Although this decision involves the relationship between an insurer and a physician, at least one court of appeal in California had decided, before this decision was issued, that the principles underlying the decision also applied to the relationship between an IPA and a physician.

Insurers, health plans, IPA's and medical groups should carefully review their policies and practices concerning the termination of relationships with physicians, and should review the language of their contracts in this regard as well. These entities may wish to consider the creation of two different types of hearing procedures in light of this opinion, one relating to medical disciplinary proceedings, and another relating to administrative or financial decision making.

For more information, contact Jay Hartz at (310) 551-8164, Angela Mickelson at (310) 551-8170, Mark Reagan at (415) 875-8501 or Glenn Solomon at (310) 551-8179.

Correction: In the April issue of *Health Law Perspectives,* we referred to a client of the firm as CCN Managed Health Care, Inc. The correct name of the firm, which is the largest preferred provider organization in the country, based on number of enrollees, is CCN Managed Care, Inc. We apologize for the error.

Nursing Homes Targeted Under New DOJ Program

Under its new investigative program, Operation Guardian, the California Department of Justice is sending teams of investigators into Medi-Cal certified skilled nursing facilities to investigate the care rendered to residents, the handling of residents' trust funds and compliance with fire and other safety codes.

The stated goal of this operation is to determine whether targeted skilled nursing facilities and/or their employees and operators, including company officials, have committed criminal elder abuse or neglect or fraud. These investigations may lead to criminal prosecution of both facilities and individuals.

Investigative teams will include an investigator, auditor and registered nurse with geriatric training from the state Bureau of Medi-Cal Fraud. Teams may also include a physician retained by the Bureau, the local ombudsman, the fire marshal and other local safety officials. Finally, the Bureau has expressly stated that the investigative team will *not* include local prosecutors, their representatives, or representatives from the Department of Health Services (DHS). In addition, these teams will not be accompanied by the press.

The California Association of Health Facilities (CAHF), an HLB client, has been actively involved in assisting facilities to prepare for and handle these unannounced investigations, which are beginning in the Los Angeles area and will move on to San Diego, the Northern California Bay Area, Sacramento, Orange County and the Inland Empire Area shortly.

HLB attorneys have worked closely with CAHF to provide guidance to facilities through workshops and other means. The following guidelines have been developed to assist facilities under investigation:

1) Despite the intrusion of investigators, facilities need to try to ensure that any investigation results in minimal disruption to the care and treatment of its residents.

2) At the outset, the facility should have a designated representative, either the administrator or director of nursing, to assist the investigator and protect the facility's interests. This representative should also take notes documenting any verbal conversations and a listing of documents requested by the investigators. In addition, facility counsel should be notified immediately and should be accessible to the facility throughout the duration of any investigation.

3) Investigators are entitled to review any and all medical and financial records with regard to the provision of care. However, they do not have the absolute right to remove original records from the facility without a subpoena or warrant. While the investigators may claim that they are entitled to seize the original records under the "plain view" doctrine (an exception to the Fourth Amendment of the United States Constitution), they should be reminded that facilities are required to maintain residents' original medical and financial records at the facility. The facility representative should then offer to copy any and all requested records.

4) It is likely that the investigators will seek to interview residents or even employees. The facility should be careful not to discourage cooperation with the investigators, but rather should inform residents and employees that they have right to agree or refuse to be interviewed.

5) Facilities should ask for documentation concerning the investigation team's findings. The Bureau has indicated that it will not conduct a formal "exit conference," but that it will provide some form of feedback to the facility.

For more information, contact Jay Hartz in our Los Angeles office at (310) 551-8164, or Mark Reagan in our San Francisco office at (415) 875-8501.

Court of Appeal Voids Healthcare District Lease

A healthcare district's suit seeking to void contracts with two nonprofit organizations cannot be barred by a statute of limitations, a state appellate court has ruled in a case of first impression, reversing a lower court decision.

The case involved Grossmont Healthcare District, which sought to recover possession of a publicly-owned hospital and related assets that the district leased and transferred in 1991 to two private nonprofit corporations—San Diego Hospital Association (SDHA) and Grossmont Hospital Corporation (GHC) under three written agreements made under the provisions of the state Local Health Care District Law. GHC is a private nonprofit corporation formed to operate the hospital under a 30-year lease. SDHA, also a private nonprofit corporation, is the parent of a multi-hospital health care system in San Diego.

In its complaint, the district alleged that the agreements are void because at the time they were executed, the district's chief executive officer, its general counsel and all five members of its board of directors had personal financial interests in the agreements in violation of conflict of interest law, specifically, Government Code Sec. 1090.

In response to the complaint, GHC and SDHA filed a motion for summary judgment, on the ground that the action was time-barred.

The district filed a cross motion, arguing that there was no merit to the statute of limitations claim made by GHC and SDHA because such limitations are barred under the "no limitations" rule in *Hoadley v. San Francisco* ((1875) 50 Cal. 265), referred to as the *Hoadley* rule. Under the *Hoadley* rule, no statute of limitations will apply to bar a state governmental entity's action to recover an interest in public trust property transferred to or claimed by a private party where the claimed private interest is challenged on the ground it is invalid by law. The district argued that the *Hoadley* rule applied because the district was seeking recovery of an interest in public trust property—the hospital and related assets.

The superior court ruled in favor of SDHA and GHC, finding that the *Hoadley* rule did not apply in part because the court found no case authority in which the *Hoadley* rule superseded state statutes of limitations.

The appellate court reversed the lower court's ruling, finding that the *Hoadley* rule does apply to this case and bars a statute of limitations defense in such an action as a matter of law and sound public policy.

Specifically, the court rejected GHC and SDHA's argument that the *Hoadley* rule is superseded by Code of Civil Procedure Section 345, which states in part that "[t]he limitations prescribed in this chapter apply to *actions brought in the name of the state or county or for the benefit of the state* or county in the same manner as to actions by private parties."

"In our view, the issue presented reduces not to whether Code of Civil Procedure Section 345 supersedes the *Hoadley* rule in the instant action, but whether the *Hoadley* rule supersedes or (to borrow the card-playing metaphor used by the [lower] court in its memorandum decision) "trumps" Code of Civil Procedure Section 345" and various other statutes of limitations, the court said. The court ruled that the *Hoadley* rule does, in fact, supersede various state statutes of limitations in this case.

It is not uncommon for a company leasing a public hospital to employ the administrator or other key individuals, according to HLB attorney Robert Lundy. If those individuals are also involved in representing the interests of the public entity in negotiation of the lease, it creates a potential conflict of interest under Government Code Section 1090.

Hooper, Lundy & Bookman is pleased to announce that **David M. Vukadinovich** has joined our Los Angeles office. A fourth-year associate, Mr. Vukadinovich received his Juris Doctor and Master of Public Health degrees from Tulane University. The focus of his practice is Medicare and Medi-Cal reimbursement and certification, state licensing, fraud and abuse compliance and patient care and bioethics issues.

"Parties entering into leases or sales of public hospitals must be very careful in terms of arrangements made to hire key employees," he said. "It is particularly important in early discussions regarding these employees to ensure that no promises are made that might taint the transaction."

For more information, contact Mr. Lundy at (310) 551-8180.

Calendar

June 16-17 HLB attorney Ken Burgess discusses the Office of Inspector General's newly released final compliance guidance for nursing homes with Lew Morris, Deputy Inspector General, at the American Health Care Association's Focus 2000 conference in Washington, D.C.

June 18 HLB attorney Pat Hooper speaks on "Coping with Government Fraud Investigations" at the American Health Lawyers Association annual meeting in Washington, D.C.

June 21-22 HLB attorney Ken Burgess speaks with OIG representatives on skilled nursing facility compliance at an American Health Care Association conference in Las Vegas.

June 27-28 HLB attorney Ken Burgess speaks on "Resident Admission Agreements in Assisted Living" at a joint meeting of the New Jersey Assisted Living Association and the New Jersey Health Care Association in Redbanks, New Jersey.

July 25 HLB attorneys Angela Mickelson and Todd Swanson speak at the National Business Institute's Health Law Seminar in Anaheim. Ms. Mickelson will speak on "Managed Care Contracts" and Mr. Swanson will speak on "Merging and Acquiring Medical Practices."

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