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Doctor investors sue Memorial Hermann



Robert Vanzant, M.D.

This is the first part of a two-part series:

In what may be a test case in how to drive for-profit physician-owned hospitals out of business, two groups of physician-investors have sued Memorial Hermann Healthcare System for allegedly orchestrating an insurance boycott that financially drained 99-bed Houston Town & Country Hospital, and led to its sale and closure.

Town & Country Hospital, which opened in November 2005, was a physician-operated, general acute-care hospital located on a 26-acre campus in west Houston. In 2003, a group of 109 physician-investors formed a limited partnership called Stealth to build the \$65 million hospital and medical office building. Each doctor invested between \$25,000 and \$150,000 for a total of more than \$7 million.

But according to the lawsuits filed in Harris County District Court, Memorial Hermann—an eight-hospital not-for-profit system that is the largest in Houston with a 25% market share—began a concerted effort to pressure insurance companies to avoid contracting with Town & Country. By the summer of 2006, with only a handful of insurance contracts, Town & Country faced financial disaster and required additional capital to stay open.

“This hospital was our dream. We wanted choice for ourselves and our patients,” says Robert Vanzant, M.D., a physician-investor in Stealth and an assistant clinical professor at the University of Texas Health Science Center at Houston.

Rusty Hardin, a Houston attorney who represents Stealth and the 109 physician-investors, says Memorial Hermann told insurers, including Aetna, Cigna Corp., Humana and UnitedHealth Group that they would terminate their contracts or demand 25% rate increases if they contracted with Town & Country.

“If Memorial hadn’t bullied the insurers we would have succeeded,” says Vanzant, who also holds staff privileges at nearby 373-bed Memorial Hermann Memorial City Hospital in Houston. “What makes it so frustrating is that we were so close to breaking even when we folded. Things were moving in the right direction. If any of the major insurers had broken ranks and contracted with us that would have put us over the top.”

Vanzant says patients appreciated having an alternative to Memorial Hermann. “Patients were coming. They loved (that) doctors had a say in this hospital,” he says.

In a statement, Memorial Hermann spokeswoman Beth Sartori said: “This litigation was launched by the investors in an effort to deny responsibility for the hospital’s failure. The claims brought against Memorial Hermann have no merit, and we look forward to bringing this matter to a swift conclusion.”

But Richard Zook, a partner with Thompson & Knight in Houston who represents several of the largest physician-investors in Stealth, contends Memorial Hermann’s action against Town & Country is part of a larger strategy to stymie development of physician-owned hospitals in the area. More than 22 doctor-

owned hospitals are open or in the planning stages, according to the Texas Hospital Association.

“Memorial Hermann is so threatened by physician-owned hospitals that they have a massive campaign to go after them,” Zook says. “Their strategy is to deny them managed-care contracts, lobby the state of Texas to require certificate of need to build, and punish doctors who invest.”

Bernie Duco, Memorial Hermann’s chief legal officer, denies the system has such a strategy. “There were discussions in the past, not just about physician-owned hospitals but specialty hospitals,” he says.

Duco characterized Town & Country as a “significant competitive threat” because of its close proximity to Memorial City Hospital and because its physicians also admitted to Hermann hospitals.

One of these physician-owned hospitals, 64-bed Foundation Surgical Hospital, Bellaire, filed a lawsuit in June against its management company over breach of contract. Physician-owned hospitals in the area include University General Hospital, Houston; 64-bed North Cypress (Texas) Medical Center; and Patients Medical Center, Pasadena.

“All physician hospitals that don’t have the protection of a big entity (large healthcare system) are being subjected to this kind of pressure from Memorial,” Hardin says.

After Medical Properties Trust, a Birmingham, Ala.-based real estate investment trust that owned Town & Country, terminated Stealth’s lease on Oct. 23, 2006, the trust began to discuss selling the hospital to several large hospital systems, court documents state.

In early January, Memorial Hermann purchased Town & Country and an adjacent medical office building for \$70 million. Two weeks later Memorial Hermann closed Town & Country.

On June 1, Zook filed the first lawsuit against Memorial Hermann. On June 18, Hardin filed the second lawsuit. Last December, Zook sued the hospital’s general partner, West Houston GP, for gross mismanagement. The state court trial against Memorial Hermann is scheduled to begin in late January 2008, Zook says.

“Doctors lost everything they invested and they are on the hook for a \$3.5 million loan from a bank in Houston,” Hardin says.

Meanwhile, on June 8, Memorial Hermann filed a federal lawsuit against Stealth asking the court to rule that the hospital system acted appropriately. Specifically, Memorial Hermann is asking the court to find it is free to enter into exclusive or semiexclusive contracts with insurers “even if the effect of such contracts is to exclude Stealth from contracting with one or more insurers.”

The Texas attorney general’s antitrust department is also investigating Memorial Hermann. Duco says Memorial Hermann has received information requests from the attorney general, but he denies Memorial Hermann tried to organize a boycott.

The physicians also claim Memorial Hermann removed some of them from committees and staff positions, terminated certain privileges of their practice at the hospital and threatened to terminate medical staff credentials at system hospitals.

Duco also denies Memorial Hermann issued any threats against physician-investors in Town & Country. “To my knowledge, most remained on the medical staffs. There was no effort to remove physicians,” he says. Stealth contends the campaign to destroy Town & Country was directed by Dan Wolterman, Memorial Hermann’s president and chief executive officer. Vanzant told *Modern Physician* that Wolterman met with him in 2003 and was told what would happen if he invested in Town & Country.

Wolterman said he had a fiduciary responsibility to see Memorial Hermann was not hurt by Town & Country, Vanzant says. "He talked about decredentialing investing doctors, creating no-compete zones with insurers and undercutting prices. I told him that is not a way to treat a partner (doctor) in caring" for patients.

Duco acknowledges the meeting occurred, but "nothing like that was said" by Wolterman.

But Zook says Memorial Hermann went far beyond normal business practices in competing against the fledgling Town & Country Hospital. "This is a simple story. A bunch of doctors wanted to create their own hospital. Once opened, the Goliath, Memorial, did everything it could to drive them out of business and hurt the doctors. They succeeded. They closed the hospital and stymied competition," he says.

Hardin says the physician-investors built the hospital not to just make money. "They wanted to have a hospital that paid more attention to the healthcare professions," he says. "They felt Memorial had become a bottom-line decisionmaking place, where medical decisions are made by nonmedical people. When it went under it was a tremendous blow to them."

Zook says legal and healthcare experts nationally are waiting to hear what the court says about Memorial Hermann's actions. "Can Memorial Hermann and other systems engage in this kind of activity? It is a battleground and test case," he says. "If Memorial can do this, this sends a message to other doctors that if you try and go against us, we will squish you like a bug."
