

Governor Cuomo Revisits Pilot Program for Private Business Corporations to Own and Operate Hospitals in New York

February 2014

New York is set to revisit the debate regarding the private ownership of hospitals. On January 21, 2014, Governor Andrew Cuomo released his Executive Budget, which again calls for the implementation of a pilot program (“Pilot Program”) to allow certain investor-owned corporations to own and operate hospitals and other designated health care facilities. The Pilot Program is found in the 2014-2015 New York State Executive Budget, Health and Mental Hygiene Bill, Part A, Section 12. Similar to last year’s proposal,¹ the purpose of the Pilot Program is to “assist in restructuring health care delivery systems by allowing for increased capital investment in health care facilities.”² This year’s proposal, however, does provide for some significant changes. The governor’s 2014-2015 Executive Budget, which the governor is statutorily required to submit to the legislature under Article VII of the New York State Constitution, is not open for public comment.³ The Executive Budget serves as a blueprint for what the governor would like the New York State Legislature to consider in its yearly budget legislation. The 2014-2015 Executive Budget may be viewed [here](#).

History

New York has strictly regulated the practice of medicine and the delivery of health care within its boundaries. One particular restriction, which has periodically been subject to debate over the years, is the statutory requirement that all owners of a corporation that operates a for-profit hospital be natural persons (i.e., human beings and not corporate entities, which are permitted in other states).⁴ The reasons for this law include the view that the provision of hospital care is a charitable activity and that there must be transparency and accountability as far as the owners of hospitals are concerned. This prohibition has essentially prevented investor-owned corporations from directly owning and operating hospitals in New York.

¹ For a discussion of last year’s proposal, see Jeffrey H. Becker & Vinay Bhupathy, *Proposed Pilot Program: Business Corporations to Operate New York Hospitals*, Epstein, Becker & Green, P.C. (January 31, 2013), <http://www.ebglaw.com/showclientalert.aspx?Show=17009>.

² *Proposed* – New York Public Health Law §2801-a(17)(a).

³ N.Y. Const. art VII §2.

⁴ New York Public Health Law §2801-a(4)(e).

The governor's proposal to establish a pilot program last year did not find the needed support in the New York State Legislature and ultimately was not included in the enacted budget. State legislators were concerned that corporate ownership of for-profit hospitals would result in the elimination of underperforming services, which would harm underserved communities.⁵

The Pilot Program maintains much of the same structure as last year's proposal and would suspend the restrictions normally applicable to owners and operators of hospitals for Pilot Program participants. This proposed modification of New York law would allow investor-owned entities to directly invest in a hospital without the requirement that all shareholders or members of a for-profit owner or operator be natural persons.⁶

Carry Over from the 2013-2014 Pilot Program

The 2014-2015 Pilot Program retains certain provisions from the governor's previous proposal, including the following:

- The Commissioner of Health ("Commissioner") is to establish the Pilot Program under New York Public Health Law §2801-a.
- To become an owner or operator in the Pilot Program, business corporations will need to affiliate, as determined by the Commissioner, with at least one approved academic medical institution or teaching hospital.⁷
- The corporate purposes and powers of the business corporations must be limited to the ownership and/or operation of specifically designated hospitals, and other health care facilities.⁸
- A business corporation's board of directors and officers must consider the same specified public health metrics when taking any actions, including: (i) "interests of patients of the hospital or hospitals"; (ii) "community and societal considerations, including those of any community in which facilities of the corporation are located"; and (iii) "the local and global environment."⁹ Consideration of these metrics will not constitute a violation of the fiduciary duty or duty of loyalty owed to the corporation or shareholders.¹⁰

⁵ Richard N. Gottfried, Letter to the Editor, *Financing Hospitals*, New York Times, April 4, 2013, at A24. (Richard Gottfried is the chairman of the New York State Assembly Committee on Health.)

⁶ *Proposed* – New York Public Health Law §2801-a(17)(c), citing current New York Public Health Law §§2801-a (3)(b), (4)(c), (4)(d), (4)(e) & New York Public Health Law §4004(3)(a).

⁷ *Proposed* – New York Public Health Law §2801-a(17)(a).

⁸ *Proposed* – New York Public Health Law §2801-a(17)(d).

⁹ *Proposed* – New York Public Health Law §2801-a(17)(e)(1).

¹⁰ *Proposed* – New York Public Health Law §2801-a(17)(e)(2), citing current New York Business Corporation Law §§ 715, 717.

- The business corporations will be eligible to receive debt financing from the dormitory authority of the State of New York (“DASNY”).¹¹

Changes to the Pilot Program for 2014-2015

The 2014-2015 Pilot Program differs from last year’s proposal in the following ways:

- The Public Health and Health Planning Council (“PHHPC”) will be authorized to approve a total of five business corporations to participate in the Pilot Program.¹² This is an increase from a maximum of two business corporations last year.
- The Pilot Program eliminates provisions specifying where in New York the hospitals that are owned or operated by business corporations must be located. There is no longer a requirement that at least one such hospital be operated in Kings County.
- Business corporations with more than 35 stockholders and corporations owned by publicly traded entities will be ineligible to participate in the Pilot Program.¹³ Last year’s proposal did not exclude such corporations from participation in the Pilot Program and even exempted corporations with more than 35 stockholders from certain reporting requirements.
- Only “principal stockholders” of a participating corporation will be required to undergo character and competency review by the PHHPC in order to own and operate a hospital.¹⁴ The previous proposal required character and competency review of all stockholders. The term “principal” is not defined.
- In addition to corporations with stockholders that are not natural persons, under the Pilot Program, hospitals may be established, owned, and operated by partnerships or limited partnerships whose members are not natural persons, after approval by the PHHPC.¹⁵ The 2013-2014 proposal omitted partnerships from owning stock of participating corporations.

Unanswered Questions

As was the case last year, the governor’s current proposal leaves certain questions unanswered, including the following:

- 1) What does “affiliate” with an academic medical institution mean?

¹¹ *Proposed* – New York Public Health Law §2801-a(17)(b).

¹² *Proposed* – New York Public Health Law §2801-a(17)(a).

¹³ *Id.*

¹⁴ *Proposed* – New York Public Health Law §2801-a(17)(c), citing current New York Public Health Law §2801-a(3)(b).

¹⁵ *Proposed* – New York Public Health Law §2801-a(17)(c) citing current New York Public Health Law §2801-a(4)(d).

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- 2) How will the participating business corporations recoup their investment, and will they be permitted to make profit distributions to their owners?
- 3) Will the Pilot Program garner interest with the numerous restrictions placed on participants?
- 4) If the proposed Pilot Program is a success, will that lead to a future loosening of current restrictions and an extension of the program to a greater number of facilities?
- 5) If the Pilot Program is not successful, what will happen to the business corporations that made investments and the capital that they have invested?
- 6) What is the meaning of the new partnership option?
- 7) What effect will the Pilot Program and its possible future expansion have on the existing not-for-profit hospitals in New York?

As noted above, the governor's Executive Budget is not open for public comment and has already been submitted to the New York State Legislature, which is currently engaged in drafting the 2014-2015 budget. Contacting your New York State legislator will be the most direct avenue to comment on the governor's proposals.

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*For additional information about the issues discussed in this Client Alert or if you would like to discuss how the Pilot Program may affect your business, please contact **Jeffrey H. Becker, Linda V. Tiano**, or the Epstein Becker Green attorney who regularly handles your legal matters.*

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