

# -- SENATE FLOOR ALERT --

## SUPPORT SB 959 (Lieu)

California Coalition on Workers' Compensation  
California Manufacturers & Technology Association  
California State Association of Counties  
California Trucking Association  
California Retailers Association  
California Restaurant Association  
California Self-Insurers Association  
National Federation of Independent Business  
Western Home Furnishings Association  
North Bay Schools Insurance Authority  
Regional Council of Rural Counties  
California Grocers Association  
Schools Insurance Group  
Association of California Insurance Companies  
California Association of Joint Powers Authority  
CSAC Excess Insurance Authority  
Employers Group  
Schools Insurance Authority  
County of San Bernardino  
Morehouse Foods, Inc.  
Actief Case Management, Inc.

American Insurance Association  
San Diego and Imperial County Schools JPA  
Seawright Custom Precast, Inc.  
iUnlimited Investigative Services  
Sedgwick Claims Management Services, Inc.  
Aerospace Dynamics International, Inc.  
EME International  
Gallagher Bassett Services, Inc.  
Nordstrom  
PPG Aerospace  
Marriott International, Inc.  
Pacific Athletic Wear, Inc.  
Grimmway Farms  
TRISTAR Risk Management  
Costco Wholesale  
The Boeing Company  
FedEx Corporation  
Western Propane Gas Association  
IBA West  
Indio Chamber of Commerce

DATE: May 9, 2012

RE: SB 959 (Lieu) – Spinal Surgery Implants: Double Payment Repeal  
**SUPPORT**

The businesses, public entities, and statewide associations listed above are pleased to **SUPPORT SB 959 (Lieu)**, which would repeal a provision in state law that allows for the double payment of implantable medical devices, instrumentation, and hardware that is commonly used in certain spinal surgery procedures.

### **BACKGROUND**

Medical services in the workers' compensation system are reimbursed according to the Official Medical Fee Schedule (OMFS). The OMFS for hospital inpatient services is adapted from the Medicare payment system for inpatient services furnished by acute care hospitals. Payment is based on the Diagnosis Related Group (DRG) that applies to the patient (DRGs are based on diagnosis, co-morbidities, and surgical procedures performed).

California pays 120% of the Medicare allowance for DRGs which, without debate, is designed to incorporate the cost the hospital stay, including any medical devices, instrumentation, or hardware used in a surgical procedure. However, California law allows for *separate payment above and beyond the DRG* for devices, hardware, and instrumentation used in complex spinal surgeries. This payment, known as a "pass-through", is technically a double-payment because it allows the hospital to pass along the cost of bill a device, instrumentation, or hardware to employers even though the cost is technically taken into consideration when setting the reimbursement level under the DRG.

## **DOCUMENTED PROBLEMS**

Recent stories in the Wall Street Journal have reinforced through what nearly a decade worth of research by the RAND Institute for Civil Justice and Health (RAND) has determined – that statutorily-mandated double-payment for certain medical devices, instruments, and hardware creates incentives for bad behavior on the part of medical providers and service providers in the workers' compensation system.

### *Overpayment*

RAND has conducted multiple detailed studies on the double-payment of spinal surgery devices, instrumentation, and hardware. The first analysis, completed in 2003, concluded that "the standard allowance should be sufficient and that the pass-through was unnecessary". The second analysis, completed in 2005, confirmed the results of the first study.

The analysis conducted by RAND is important, because it refutes the arguments advanced by opponents to a repeal of the spinal surgery "pass through". Opponents argue that workers' compensation is different than Medicare and the DRG, which is developed for Medicare, does not adequately account for the added complexity of procedures performed in the workers' compensation system. As such, they argue that the double-payment is necessary to preserve access to spinal surgeries for injured workers. The RAND analysis takes this argument head on:

"Our comparative analysis of Medicare and workers' compensation spinal surgery discharges shows that on average workers' compensation patients are less costly than Medicare patients and have a shorter length of stay. The DRG-mix adjusted Medicare cost per discharge is about 14% higher than the cost per discharge for workers' compensation patient.

The payment simulation suggests that 1.20 times the Medicare rates had been used to pay for spinal surgery discharges in 2003, total OMFS payments would have exceeded estimated costs." (*Payment for Hardware Used in Complex Spinal Procedures under California's Official Medical Fee Schedule for Injured Workers, RAND 2005*)

### *Overutilization*

Overpaying for procedures is undesirable, but the real harm comes in the form of negative medical outcomes for injured workers resulting from overutilization of spinal surgery devices, instrumentation, and hardware. On this subject, RAND notes:

"Finally, when we looked at usage of hardware across patient populations and hospitals, we found that the usage rates for workers' compensation patients are considerably higher than for Medicare patients for some but not all DRGs. We also found substantial variation in the usage rates for workers' compensation patients. Four hospitals used hardware 75 percent more often than would be expected based on the overall usage rates for workers' compensation patients with the same DRG mix. (*Payment for Hardware Used in Complex Spinal Procedures under California's Official Medical Fee Schedule for Injured Workers, RAND 2005*)

A recent Wall Street Journal article (attached) provides a detailed account of how consultants have helped some hospitals cash in on the high reimbursements and, in the process, intentionally inflated the cost of medical devices in order to profit even more handsomely. The story is evidence that the RAND findings have impact in the real world. Over-reimbursement leads to bad behavior that drives bad results for injured workers and high costs for employers.

## **ELIMINATING DOUBLE PAYMENT**

SB 959 eliminates the statutory authority for the double payment of spinal surgery devices, instrumentation, and hardware via the pass through mechanism. The bill will not only stop unnecessary and duplicative payments, but will also reduce the profit-motive that sometimes leads to unethical behavior by medical providers. Arguments that it will impede access to spinal surgeries simply do not stand up when weighed against the mountain of empirical evidence provided by RAND.

The businesses, public entities, and statewide associations above strongly urge you to **VOTE YES** when **SB 959** is heard in the Senate Labor and Industrial Relations Committee.



## In Small California Hospitals, the Marketing of Back Surgery

By JOHN CARREYROU, TOM MCGINTY and JOEL MILLMAN

February 9, 2012

HAWAIIAN GARDENS, Calif.—Consuelo Solorio, a middle-aged tomato-cannery employee, traveled three hours from her home in the San Joaquin Valley to have spine surgery here for an injury from tumbling off a ladder.

Her destination was Tri-City Regional Medical Center, a hospital that has developed a thriving business doing back surgery on workers' compensation patients.

It built up this business rapidly. For an operation known as spinal fusion, which joins two or more vertebrae, the small hospital billed workers' compensation insurers \$65 million in 2010, up from less than \$3 million three years earlier, state hospital discharge data show.

Helping spur the business was Paul Richard Randall, a consultant to whom Tri-City has paid millions of dollars in marketing fees. According to people familiar with his role, it was twofold: bringing surgery cases to the hospital by recruiting surgeons to operate there, and supplying metal implants for the surgeries through distributorships he owned.

The U.S. attorney in Los Angeles has investigated Mr. Randall's practices. By last August, federal prosecutors had prepared a charge that, if filed in court, would accuse him of conspiring to inflate the cost of spinal-surgery hardware and use part of the proceeds to pay kickbacks to doctors to refer workers' compensation patients for surgeries at Tri-City, according to a copy of the charge reviewed by The Wall Street Journal.

### **Spinal Fusions**

See statistics for the top 20 California hospitals ranked by the number of spinal fusions performed on injured workers from 2008 through 2010.

Mr. Randall said he is just one of a dozen spinal-implant distributors in the Los Angeles area who mark up the price of the surgical hardware they provide to hospitals, and "there's nothing illegal about what I'm doing, my lawyer tells me." As for the kickback allegation, "that's not true," Mr. Randall said.

The U.S. attorney's office declined to comment. The status of its investigation is unclear. A lawyer for Mr. Randall said no charges have been filed against his client.

An official of Tri-City said the hospital ended its relationship with Mr. Randall in the middle of last year, a few months after it ousted the executive who had hired him. An internal investigation involving various issues at the hospital is under way, a review that a hospital tax filing said has found numerous "improprieties."

A lawyer who is conducting the internal inquiry said the hospital didn't know that Mr. Randall was inflating the cost of spinal-surgery hardware he sold to the hospital until late in 2010, and it never has been aware of any possible kickbacks to doctors. Hospital officials also said they weren't aware of any federal investigation of the hospital or Mr. Randall.

Tri-City, a 107-bed facility just south of Los Angeles near Long Beach, illustrates a U.S. health-care trend, the increasing total bill for back surgery, that the Journal has traced in articles over the past 15 months.

In California, this trend shows up in the workers' compensation system. California employers paid \$7.1 billion in insurance premiums to cover their workers' compensation liability in 2010. Spinal-fusion surgery is a growing part of the care these premiums pay for. It accounted for 40% of inpatient hospital charges to the state workers' compensation system in 2010, up from 30% in 2001, a Journal analysis of hospital discharge data shows.

Mr. Randall, 52 years old, an entrepreneur with a collection of sports memorabilia and a yen for gambling, began his career as a hospital marketer in the mid-1990s after serving a stint in federal prison for racketeering. He was convicted of the felony in 1993 for deals that involved buying wooden shipping pallets on credit and reselling them without paying the original vendors, and was sentenced to a 21-month term.

After serving time in the Terminal Island federal correctional facility in Long Beach harbor, Mr. Randall went into business with Michael D. Drobot, the owner of another small hospital near Tri-City called Pacific Hospital of Long Beach.

A Naval officer in the Vietnam era, Mr. Drobot bought Pacific in 1997 and shifted its focus to spine care for workers' compensation patients, a clientele other hospitals weren't keen to treat because of bureaucratic and legal headaches of dealing with insurers and uncertainties about payment.

For a decade, Messrs. Randall and Drobot operated a business that arranged for magnetic resonance imaging, or MRI, services. Mr. Randall also introduced Mr. Drobot to doctors to increase spine-surgery business at Pacific Hospital, according to a person with knowledge of the arrangement. Asked about that, Mr. Drobot said through a spokesman that Mr. Randall introduced "a few" doctors.

He said Mr. Randall was paid \$25,000 a month to run the MRI business plus a share of profits. For a time, the two men also co-owned a weekend retreat in Bullhead City, Ariz., along with a doctor.

Mr. Drobot created several businesses focused on workers' compensation patients: a van service to shuttle patients, a provider of Spanish interpretation and a distributorship of metal implants used in back surgery. His hospital became one of the most prolific spine-surgery facilities in California. Between 2001 and 2010, Pacific performed 5,138 spinal-fusion surgeries on workers' compensation patients, according to state hospital discharge data, and billed \$533 million for them—three times as much as any other hospital in the state, including much larger ones.

Through his spokesman, Mr. Drobot said the number of surgeries was even higher than that tally but the money received for them was lower, just \$231 million. Insurers often fight hospitals over billings and end up paying less.

After a business dispute between the two men, Mr. Randall in 2008 moved to Tri-City, a hospital eight miles away that then focused on bariatric surgery.

Tri-City, which is a nonprofit institution, paid Mr. Randall more than \$3.2 million between 2008 and July 2011 as a business-development consultant, according to its filings to the Internal Revenue Service and a hospital lawyer. Mr. Randall recruited some of the same spine surgeons to Tri-City that he earlier introduced to Mr. Drobot at Pacific, according to a person familiar with the matter.

Like Pacific before it, Tri-City soon was doing many more back operations; within three years, Tri-City's billings for spine surgery on workers' compensation patients soared twentyfold to \$65 million. A lawyer for the hospital says amounts actually collected totaled just \$22.5 million.

As Mr. Drobot had done at Pacific, Mr. Randall formed spinal-implant distributorships, which purchased hardware and resold it to Tri-City hospital.

California's Workers' Compensation Division permits hospitals to bill separately for spinal implants, rather than include their cost in an overall charge for surgery, as is the case in the Medicare and Medicaid systems.

The California Workers' Compensation Institute, an insurers' group, has estimated that separate billing for implants added \$55 million in costs to the program in 2008. The workers' compensation division says it is considering modifying the system in a way that would eliminate the extra costs.

The workers' compensation division doesn't put a limit on how much a distributor may mark up the cost of implants when it sells them to a hospital, although it does restrict how much a hospital may mark up its own implant cost when it bills an insurance company.

Mr. Randall's distributorships imposed some steep markups, invoices reveal. Invoices for 16 spine surgeries at Tri-City between July 2010 and March 2011 show items for which suppliers charged Mr. Randall's distributors \$326,000, while his distributors charged the hospital \$1.1 million.

The draft charge the U.S. attorney's office prepared last year, but hasn't filed, stated that in 2010 Mr. Randall submitted to Tri-City an invoice for spinal-surgery hardware that listed the cost as \$42,467, when the actual cost of the hardware bought by the Randall distributorship was \$3,600.

The draft charge further alleged that Mr. Randall conspired to pay chiropractors and physicians kickbacks of approximately \$15,000 to \$20,000 per spinal surgery to refer workers' compensation patients for operations at Tri-City. It alleged that he "paid the kickbacks...from his profits on inflating the cost of the spinal surgery hardware" by "2-10 times the actual purchase price."

By August of last year, the federal prosecutors had prepared a proposed plea agreement for Mr. Randall. He said he hasn't signed it.

Kenneth Yood, a lawyer hired by Tri-City's board in late 2010 to do an internal investigation of various matters at the hospital, said that Tri-City isn't aware of any possible kickbacks to doctors.

He said Tri-City's board didn't become aware until the fall of 2010 that charges for spinal implants by Mr. Randall's distributor "were arguably excessive." Mr. Yood said the hospital has since made changes "to address several matters related to vendor-supplied implants," including requiring vendors to attest that they comply with all applicable laws and regulations.

Mr. Yood said his review is examining what he called "highly questionable transactions" a former chief executive "caused the hospital to enter into with third-party vendors, including Paul Randall." The former CEO, Arthur Gerrick, was removed for misconduct in April, according to the hospital's general counsel, Beryl Weiner.

Mr. Gerrick "categorically denies" all Tri-City allegations against him, his lawyer said.

Messrs. Gerrick and Weiner were partners in a company that managed Tri-City for several years through the end of last year. The nonprofit hospital paid this management company about \$3.4 million a year.

Mr. Weiner said Tri-City ended its relationship with Mr. Randall last summer, after receiving an anonymous letter that described his criminal past.

The chairman of Tri-City's board, Brian Walton, said that "over the past three years, the hospital went through some traumas. As best we can, we've been trying to clean up the mess.... Obviously, we could concede that there are things that went on in the past that could be upsetting."

Ms. Solorio, the tomato-cannery employee, is one of hundreds of injured workers treated at Tri-City during those three years.

She worked as a cleaner in a Rio Bravo Tomato Co. cannery in the San Joaquin Valley, an area home to many Hispanic field workers. Over the past decade, at least 550 workers from the region had spinal fusions at the two Long Beach-area hospitals Mr. Randall was connected with, chiefly at Pacific, according to state discharge data.

Ms. Solorio lived with her husband, Rafael, and a son in a brown bungalow around the corner from a trailer park in Shafter, an impoverished town along a stretch of rural highway. She injured her neck falling off a ladder at work, according to Mr. Solorio, a Mexican-born ranch hand who speaks little English.

An attorney who handled her workers' compensation claim, William Berry, said he first referred her to a local chiropractor and then to a spine surgeon, who, Mr. Berry said, didn't recommend surgery.

At some point, according to several people familiar with the matter, Ms. Solorio became a patient of Edward C. Kolpin, a surgeon who operated at both Pacific Hospital and Tri-City. Dr. Kolpin scheduled surgery for the 52-year-old worker at Tri-City, which is 150 miles from her home.

The surgery on Oct. 6, 2010, joined four neck vertebrae, in what is known as a three-level cervical fusion.

State hospital discharge records show Dr. Kolpin used a bone-growth product that accelerates fusion, called bone morphogenetic protein. The Food and Drug Administration approves this substance only for a particular type of surgery of the lower spine; the FDA warned in 2008 against using it on the neck area because of reports of life-threatening tissue swelling that compressed patients' airways.

The day after the surgery, Ms. Solorio experienced difficulty breathing and died. The surgeon, Dr. Kolpin, didn't return calls and text messages seeking comment.

A surgeon who assisted in the surgery, Khalid Ahmed, who also operates at Pacific, said the outcome had nothing to do with the surgery, which he described as "well performed."

State hospital discharge data show Tri-City billed \$177,138 for Ms. Solorio's surgery. Tri-City, citing patient privacy, declined to comment other than to say it regrets any instances "in which patients expire while in the hospital or thereafter."

By August 2011, Mr. Randall said, he was back to doing spine-surgery marketing work for Mr. Drobot at Pacific Hospital of Long Beach.

Mr. Randall said he signed a \$100,000-a-month marketing agreement with Mr. Drobot—technically between Mr. Drobot's spinal-implant distributorship and a Randall marketing firm—under which Mr. Randall is to provide services such as "recruiting surgeons to the medical staff of hospitals that use" implants Mr. Drobot distributes. The Journal reviewed a copy of the purported contract.

Mr. Drobot said through a spokesman that he didn't recall entering into any such contract and that he didn't believe the signature on the document was his.