



August 17, 2007

Honorable Sam Johnson
U.S. House of Representatives
Washington, DC 20515

Dear Congressman:

As you requested, I am pleased to provide information on CBO's estimate of the budgetary impact of section 651 of H.R. 3162, the Children's Health and Medicare Protection Act of 2007.

Under current law, physicians are prohibited from referring patients to a provider of health care services in which the physician has a financial interest. There are exceptions to that prohibition, however, for referrals to hospitals that serve predominantly rural populations or to a hospital in which the physician's financial interest is in the whole hospital (in contrast to an interest in some discrete component of the hospital).

Section 651 would require physician-owned hospitals to meet certain requirements to continue qualifying for an exception from that prohibition. Those requirements would include specific limits on the percentage of the hospital that physicians may own and on the allocation of financial returns on those investments, and would have the effect of limiting the number and size of physician-owned specialty hospitals. CBO estimates that enacting that provision would reduce Medicare spending by \$0.7 billion over the 2008-2012 period and \$2.9 billion over the 2008-2017 period.

In recent years, the number of physician-owned specialty hospitals (which generally provide orthopedic, cardiac, or surgical services) has grown rapidly. CBO expects that growth will continue, partly in response to real declines in Medicare's payment rates for physicians' services under the sustainable growth rate system. Accordingly, CBO projects that, under current law, payments to physician-owned specialty hospitals will grow from about \$1.3 billion in 2007 to more than \$2 billion by 2011, and continue to grow in future years.

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Under section 651, however, CBO would expect a significant shift in utilization from specialty hospitals to other facilities. In general, the change in the type of facility would have little net budgetary effect. However, CBO estimates that savings would result from lower use of outpatient services that would be shifted to other facilities and from lower payment rates for surgical services that would be provided in ambulatory surgical centers (ASCs).

Analyses conducted by the Medicare Payment Advisory Commission and the Department of Health and Human Services have concluded that, on average, Medicare spends more—especially for outpatient services—for patients treated in physician-owned specialty hospitals than it would if those patients were treated in other hospitals or ASCs. Those findings are supported by several studies reported in peer-reviewed journals. Based on that literature, CBO estimated that spending for outpatient services would be reduced by about 15 percent for patients who will be treated, under current law, in orthopedic and surgical hospitals that would be affected by section 651. That reduction in spending for outpatient services accounts for \$0.5 billion of the estimated \$0.7 billion in savings for section 651 over the 2008-2012 period and \$2.3 billion of the estimated \$2.9 billion in savings over the 2008-2017 period.

Medicare's payment rates are higher for hospitals than for ASCs for surgical services that can be provided by both. CBO expects that most of the surgical hospitals affected by section 651 would instead be organized as ASCs and would receive the lower ASC payment rate. That change accounts for the remaining \$0.2 billion of the estimated savings over the 2008-2012 period and \$0.6 billion of the savings over the 2008-2017 period.

I hope this information is helpful to you. The CBO staff contact for further information is Shinobu Suzuki.

Sincerely,



Peter R. Orszag
Director

cc: Honorable Charles B. Rangel
Chairman
Committee on Ways and Means

Honorable Jim McCrery
Ranking Republican