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South Dakota Case Will Be Significant Precedent for Hospital Governing Boards to Take Economic Factors into Consideration When Granting Medical Staff Privileges

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A fight over medical staff privileges between physicians and a hospital in Aberdeen, South Dakota has produced a court decision that will be a landmark in the law of hospital governance. When hospitals look beyond medical qualifications in evaluating applications for medical staff privileges, disgruntled physicians often accuse the hospital of "economic credentialing," implying that the hospital is making an economic decision and depreciating medical competence. Few court decisions have addressed a hospital board's authority to make business decisions which further the best interests of the hospital but which negatively affect a physician's staff privileges. No consistent rule of law has emerged from those cases which have considered the issue.

On January 10, 2001, the South Dakota Supreme Court issued its opinion in *Mahan v. Avera St. Luke's*. In *Mahan*, the plaintiffs challenged St. Luke's refusal to extend an application for staff privileges to an orthopedic surgeon (Dr. Mahan) who had recently joined plaintiffs' orthopedic surgery practice. St. Luke's is a private, non-profit hospital located in Aberdeen, South Dakota and the only general hospital within 90 miles. In June 1997, St. Luke's governing board closed its medical staff to new orthopedic surgeons (except those being recruited by St. Luke's) and three spine procedures.

Economic Justification For Staff Closures

Two events led to these staff closures. First, in 1996, the sole neurosurgeon practicing at St. Luke's left Aberdeen. Seeking to fill the void in neurosurgery coverage, the St. Luke's Board of Trustees passed a resolution for the recruitment of two neurosurgeons or two spine-trained orthopedic surgeons. During the recruitment process, St. Luke's learned that most neurosurgeons would not come to Aberdeen if a spine-trained orthopedic surgeon was already practicing in the area because a spine-trained orthopedic surgeon is qualified to perform back surgeries and any neurosurgeon recruited by St. Luke's would need to perform back surgeries to maintain a full-time neurosurgery practice in Aberdeen. St. Luke's governing board determined that full-time neurosurgery coverage was a critical community need. The board further determined that granting staff privileges to a spine-trained orthopedic surgeon would deny a neurosurgeon a full-time practice in Aberdeen. To attract and retain a neurosurgeon to serve the Aberdeen community, the board closed the medical staff for three spine procedures.

Second, in April 1997, plaintiffs announced plans to construct their own for-profit surgery center that would directly compete with St. Luke's. Plaintiffs also revealed their plans to recruit a spine-trained orthopedic surgeon who would perform spine procedures at the surgery center. Plaintiffs had previously performed all of their surgeries at St. Luke's. During only the first several months that the surgery center was in operation, St. Luke's suffered a 1,000 hour loss of operating room usage. A reduction in operating room usage is a legitimate concern for the board because a hospital's surgical staff must participate in a certain volume of procedures to maintain proficiency. In addition, the board determined that a continued drain on revenue otherwise generated by use of St. Luke's surgery suites would undermine its ability to offer certain less profitable but essential services such as pediatrics and emergency services. Thus, in June 1997, St. Luke's governing board voted to close the medical staff to general orthopedic surgeons as well as the three spine procedures. Physicians then holding privileges at St. Luke's were not affected by the staff closures. When Dr. Mahan requested an application for staff privileges, St. Luke's declined his request pursuant to the June 1997 staff closure.

Plaintiffs' Legal Theory

Plaintiffs filed suit against St. Luke's asserting claims of breach of contract and violation of state antitrust laws. The antitrust claims were dismissed before trial, and plaintiffs proceeded to trial on their breach of contract claim. Plaintiffs prevailed at the trial court and St. Luke's appealed. Relying solely on the language of the medical staff bylaws, plaintiffs argued that St. Luke's had delegated authority for medical staffing decisions to its medical staff. Thus, according to plaintiffs, the governing board lacked authority to implement the staff closures and its conduct was in breach of St. Luke's medical staff bylaws.

Supreme Court Rejects Plaintiffs' Claims

On appeal, the South Dakota Supreme Court acknowledged that medical staff bylaws constitute a contract between the hospital and its medical staff under South Dakota law. However, the Court soundly rejected plaintiffs' claim that the governing board had delegated authority over medical staff decisions to the medical staff. The Court began its analysis by noting that South Dakota law provides that the affairs of a non-profit corporation "shall" be managed by a board of directors. The Court then focused on St. Luke's corporate bylaws. Examining the corporate bylaws, the Court found that "the medical staff has no authority over *any* corporate decisions unless specifically granted that power in the Corporate Bylaws or under the laws of the State of South Dakota" (emphasis in original). The Court concluded that the corporate bylaws delegated to the medical staff only the responsibility for making recommendations to the Board regarding the professional competence of staff members and applicants for staff membership. The Court found that the trial court misconstrued this limited grant of authority to the medical staff as a delegation of authority and control over staff appointments.

To further support its holding, the court characterized plaintiffs' claims as a challenge to an administrative decision, not a medical staffing decision. Under the Court's analysis as well as general principles of corporate law, administrative decisions affecting the business of the corporation are properly reserved to the hospital's governing board, not the medical staff.

Impact Of *Mahan* Decision

Read narrowly, the holding in *Mahan* is based on an interpretation of St. Luke's corporate bylaws and medical staff bylaws and an analysis of the legal relationship between them. However, the Court went to great lengths to emphasize that the affairs of a hospital corporation are managed by a board of directors and that such directors "possess a large amount of discretionary power within the limits of their legal authority, and in the exercise of business judgment in the performance of their duties." The Court made this pronouncement having found that St. Luke's implemented the staff closures based on economic factors. Statutes exist in some states addressing a hospital board's authority to consider economic factors in connection with medical staffing decisions. These statutes may affect the outcome of similar cases. While the holding in *Mahan* rests on an analysis of the language of the hospital's corporate bylaws and its medical staff bylaws, the opinion strongly intimates that a private hospital may properly consider economic factors and the hospital's legitimate business objectives when evaluating a request for medical staff privileges.

Gardner, Carton & Douglas was co-counsel for Avera St. Luke's during proceedings before the trial court. For more information on the Mahan decision, or other questions concerning the denial or revocation of medical staff privileges, please contact Tom Campbell at (312) 245-8425 or John D'Attomo at (312) 245-8554.

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