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Hijacking at the Hospital

Purchasing groups created to hold down health costs seem to be holding up patients instead.

By PABLO LASTRA

A Texas engineer designed a syringe with a needle that automatically retracts after one use, a design that could save so many lives among

healthcare workers that a medical workers' union was screaming for it. But the sales teams trying to sell the improved syringes to hospitals were routinely shown the door without even getting to make their pitch.

The sales crew for a California inventor got the same treatment. He'd developed a far more accurate version of the device that measures the levels of blood oxygen — an advance with the potential to save many newborns every year. But despite the support of doctors' groups, hospitals across the United States were denied the chance to buy his revolutionary product.

By comparison, new software to help hospitals keep up with medical supply needs doesn't sound so dramatic. Nonetheless, its developer says the software could save healthcare consumers in this country up to \$80 billion a year. But when the software company went looking for funding to launch a business based on the new system, the bank turned it down for what seemed like bizarre reasons. Perhaps a more plausible explanation: The bank had a business relationship with an investment firm closely tied to a giant hospital supply entity, one that controls close to a third of all the hospital supply business in the United States — and that stood to lose hugely by the introduction of such software.

The common link in all these cases is Novation, a North Texas company that, while little known to the average person, has become the largest broker of hospital and medical supplies in the country, wielding enormous influence over the lives of patients, the safety of hospital workers, and the zooming costs of healthcare in this country. But it's also a giant in trouble. Several small medical supply manufacturers that say they have been squeezed out of the market by Novation are lining up to sue, and the company has already paid out millions of dollars in settlements. Congress is in its third year of investigating Novation's activities. At least one state attorney general is investigating the company. And now the company is a target of a Dallas-based investigation by the U.S. Attorney's office into massive allegations of Medicare fraud — a probe that has been hampered by the deaths, within the last 18 months, of two of the prosecutors involved in it.

The irony is that Novation and other entities like it — called group purchasing organizations — were invented to help hospitals save money. But instead of saving patients money, many people



Shaw: 'If you pay anybody a fee ... to try to influence a purchase, that would put you in prison in any other industry.'



Novation claims it saves member hospitals \$1 billion a year.



U.S. Sen. Herb Kohl of Wisconsin co-authored legislation that would have strictly regulated GPOs like Novation.

charge, Novation, in effect, is working on behalf of manufacturers and suppliers, helping them — and Novation itself — to make as much money as possible, to the detriment of taxpayers and the healthcare-buying public. Moreover, a recent deal involving a publicly traded partner of Novation has raised more concerns about its position in the healthcare industry, which verges ever closer to a monopoly. All while prices for medical supplies — paid for by insurers, patients, and taxpayers — continue to escalate at a rate far outpacing inflation.

“It’s a bad deal for consumers,” said Bud Weinstein, a University of North Texas professor of economics who has studied the GPOs on behalf of smaller manufacturers. “They claim that they save consumers money, but healthcare costs are rising at twice the rate of inflation.”

Novation and other GPOs were given the right by Congress to accept payments that would be illegal kickbacks in any other industry. The end result is that groups that are supposed to be working for hospitals and patients to lower costs actually get their money from manufacturers whose natural tendency is to raise, not lower, prices and who can use their influence with the GPOs to corner the market for their products through long-term contracts worth billions of dollars. Critics compare this system to a car salesman who tells buyers that he’s working to get them a lower price, when it’s clearly against his interest to reduce his percentage-based commission. Small manufacturers claim that the GPOs, which control access to almost all hospitals, freeze them out of the market through backroom deals with medical supply giants like Tyco and Becton Dickinson.

Some Novation board members purchased stock in the companies they were supposed to be negotiating lower prices from — a clear conflict of interest. When Congress threatened to tighten up conflict-of-interest rules, they simply quit the board rather than give up the valuable stock.

How many patient-generated, taxpayer-provided, congressionally allowed dollars are ending up in Novation directors’ personal pockets? That may be the biggest kick in the pants of all: Novation won’t show the government or anyone else in the public their books — except as required by the subpoenas that arrive with increasing frequency at the company offices.

The first group purchasing organization for medical supplies in the United States was created by New York hospitals that teamed up almost a century ago. But GPOs really took off in the 1980s as healthcare costs soared due to quickly evolving technology. Many of the small GPOs consolidated to form larger buying pools that could negotiate better prices with manufacturers through combined purchasing power and economies of scale.

Today there are some 600 GPOs, wielding control over \$66 billion in healthcare supplies every year. Only about 30 have the size to negotiate significant volumes of sales, and the largest of them all is Irving-based Novation, a for-profit cooperative that claims to broker \$24 billion in sales annually. Novation and Premier, the second-place company, together control about 54 percent of all hospital purchases in the country.

In 1986, Congress passed legislation regulating GPOs, including the so-called “safe harbor” agreement that exempts GPOs from federal laws against kickbacks. The rationale was that allowing GPOs to be financed by “administrative fees” paid by suppliers would allow hospitals to spend their money on patient care. Hospitals that belong to GPOs are obligated to buy supplies from them.

Novation came into existence in 1998, when two hospital networks — VHA of Irving and the University HealthSystem Consortium based in Illinois — set it up as a joint venture. VHA is a network of around 2,200



Lipari: ‘They’re keeping us out of the market. There’s a vast number of companies ... that Novation’s monopoly is doing this to.’

nonprofit hospitals and care organizations, including large hospitals like Baylor and Yale-New Haven. UHC has only about 200 members, but they include prestigious teaching and research hospitals like Parkland in Dallas.

GPOs like Novation say that, if not for them, healthcare would be even more expensive. However, the Government Accountability Office reported to Congress that in many cases, hospitals that used GPO contracts paid more for supplies than they would if they negotiated with the vendors directly.

Fort Worth Weekly contacted Baylor, Parkland, Children's Medical Center in Dallas, and Tarrant County's John Peter Smith hospital system to ask about their experiences with the GPOs. Baylor officials said they didn't have time for interviews. Children's Medical Center officials didn't return a reporter's phone calls. JPS officials called back but didn't reach a reporter by deadline.

Anthony Hinds, Parkland's vice president for strategic sourcing, said his hospital is "very satisfied" with Novation. "Novation's position is unique — if we had to actually do the contracting for every item, we'd have to increase our staff fivefold," Hinds said. "But Novation does that for us. As long as we can validate that we're getting the best values, it saves us a lot of effort and money. From my standpoint, Novation really helps us not have to hike up our costs."

Hinds said he could not say how much money Parkland saves through its Novation contracts, but that considering other services Novation provides its members besides buying, such as evaluating products, hospitals get a good deal.

Money's not the only consideration, however. Some people believe that GPOs are costing lives as well as millions of dollars.

As many as 60,000 healthcare workers contracted serious infectious diseases from accidental needle sticks in the last decade, including an average of one a week infected with the HIV virus. When Tom Shaw of Little Elm, west of Frisco in Denton County, heard the statistics in the late '80s, he started thinking about how a syringe might work that would eliminate such risk. Shaw, an engineer by training, eventually came up with a brilliantly simple solution: a syringe in which a spring mechanism retracts the needle into the barrel once the plunger is depressed, making reuse — and accidental pokes — impossible. He started Retractable Technologies to market the invention.

At the time there were other safety syringes in the market, but the mechanisms were more complicated, weren't completely foolproof, and could be modified for repeated use. However, when Shaw began trying to market his line of safety syringes in 1997, he found he couldn't even get in the door to show the products to hospitals, despite some clear advantages over competing products and the preference expressed by healthcare workers who had tried them. The reason, it turned out, was that the hospitals he tried to sell to were on GPO contracts — and were required to purchase from the large manufacturers that sold through the GPO, like \$5 billion-a-year syringe giant Becton Dickinson, which controls 90 percent of the syringe market in this country. Shaw criticized the system in the press and to legislators while at the same time trying to get on board with the GPOs by submitting bids. But the methods of doing business that the GPOs demanded seemed like bribery to him.

"If you pay anybody any fee, administrative or otherwise, to try to influence a purchase, that would put you in prison in any other industry," he said. "With the safe harbor [provision], the major manufacturers can pay GPOs to keep [other companies] out of the hospitals, and the GPOs make a lot of money."

When Novation finally looked at another of Retractable's products — a safer device for taking blood samples — the GPO suggested to Shaw that it could carry his company's product under its private label, Novaplus. Novation officials told him that by labeling the product as Novaplus, they could raise the price per unit to \$1 from the 27-cent bid that Retractable had submitted, and the two companies would share the profits from the huge markup. According to the lawsuit Retractable eventually filed, a similar offer came from Premier, the second-largest GPO, which invited Retractable to attend a conference for suppliers, where \$25,000 would buy Shaw not only advertising but also a "private dinner" with Premier executives and a small-group meeting with hospitals. Shaw rejected both deals and continued to rail against GPOs, eventually getting the attention of Congress.

Nick Rudikoff is a field researcher with the Service Employees International Union, which represents many nurses and other medical care workers and also runs a web site called Novation Watch. He said the union will

oppose GPOs, especially Novation, as long as they continue to fail to deliver on their promise of lower prices and safer products.

“We believe that Novation’s ... business practices exclude some of the most innovative medical devices like safer needles, while the costs [of resulting injuries and claims by workers] are passed on to healthcare purchasers,” he said. “The infuriating part is our members don’t mind putting their lives on the line, but hospitals aren’t doing all they can to protect our workers. It’s completely unacceptable that the hospitals can’t buy these technologies because they are locked in a contract.”

Shaw agreed. He said that even though his syringes cost a few pennies more than competitors’, the cost is minimal compared to the risk of exposing healthcare workers to deadly disease. Retractable now has a contract with Novation, but Becton Dickinson still sells far more needles thanks to its lower price and volume agreements with hospitals, even though clinical tests show Becton Dickinson’s model resulted in more needle sticks. Shaw said Novation pushes Becton Dickinson’s syringes because they make more money off them.

“They’re killing nurses,” he said. “Novation doesn’t tell them they’re not getting a safe needle. But they’re moving a lot of them, and they’re collecting a lot of fees. Nurses don’t complain because they care for other people, not themselves.”

When asked about Retractable’s charges, Lynn Gentry, director of public relations for VHA, a Novation co-owner, said that small manufacturers like Retractable have gotten the attention of the media, but that for all its complaints, Retractable is now under contract with Novation and hospitals are free to buy its syringes.

Shaw and others said that his company’s experience makes it clear that the basic problem with GPOs won’t be fixed until the organizations are forced to stop taking fees from manufacturers.

“You work for the man who pays you,” Shaw said. GPOs aren’t really group purchasing organizations, working to help the buyer, he said — “They’re group sales organizations. They’re moving sales for major manufacturers, who pay bribes they call ‘administrative fees.’ Becton Dickinson pays to keep us out of hospitals — and that would put them in prison if they didn’t have a safe harbor provision.”

Ironically, Retractable, which is struggling to compete in the American market, is succeeding in China, which is licensing its safety syringe design with the intention of manufacturing 400 million syringes a year. Retractable also scored a major contract with the U.S. government to provide seven African countries with safe needles to help prevent transmission of AIDS.

“We can sell in communist countries because it’s very dangerous” for bigger companies “to try to pay bribes over there,” he said. “I don’t know if there’s a safe harbor in China to pay bribes to put products in the market that aren’t safe. Americans fund the development of this technology, but they don’t get to use it because of all the illegal activities going on here.

“The system is crooked — even Japan and Germany can’t get into the American medical supply market,” he said, because “the market here is already owned and paid for by the American companies.”

And hospitals are part of the problem, not innocent victims of the scheme, Shaw said. Since GPOs are set up as cooperatives, their revenue from administrative fees is shared with member hospitals.

Several sources told the Weekly that most hospitals bill insurance companies and Medicare or Medicaid for the full price of supplies bought through GPOs. When the hospitals later receive the fee income that provides a substantial discount on those prices, the resulting cost reductions are not passed through to those who were charged full price. Some question whether that practice constitutes insurance and Medicare and Medicaid fraud.

“What they [hospitals] want is two sets of invoices, one that says that they paid a [higher] price, that they turn over to the insurer or the government,” Shaw said. “Which is not what they really pay once they take into account the reimbursements and rebates and benefits they get from GPOs.”

Joe Kiani couldn’t get his product into American hospitals even though doctors were asking for it and babies’ lives were at stake.

An Iranian immigrant, Kiani took out a second mortgage on his California home in 1989 to start a company called Masimo. His mission was developing a better pulse oximeter, the device that measures oxygen in the blood and is critical to monitoring newborns. Independent testing showed that Kiani's version of the device virtually eliminated a problem plaguing earlier oximeters — false readings of blood oxygen levels that occur as a result of patient movement. A false alarm could result in a nurse administering too much oxygen to a baby, resulting in eye damage. On the other hand, if a nurse, after getting false readings, then disregarded a true reading, the result could be lack of oxygen to the brain, followed by brain damage. According to articles in The New York Times, doctors who tried Kiani's product found it far superior to the most popular oximeter, manufactured by Nellcor, a unit of Tyco International, a \$40 billion-a-year scandal-plagued conglomerate.

Like Shaw, Kiani found that hospitals would not buy his product because Masimo did not have a contract with a GPO. According to court filings, when Masimo approached Premier, the GPO's own product-review process concluded that the new oximeter was superior to Nellcor's. Nonetheless, Premier's contract for pulse oximetry went to Nellcor — which, along with its parent company, was paying millions of dollars in fees to Premier and even investing in Premier's "Innovation Institute." Nellcor also got a multi-year contract with Novation.

Masimo and Retractable both took on the system through the courts.

Retractable filed a federal lawsuit against Novation, Premier, Becton Dickinson, and Tyco in Texarkana federal district court in January 2001, alleging that "the defendants combined or conspired to eliminate or lessen competition and to acquire and maintain monopoly power among hospitals and healthcare technology providers." The antitrust complaint stated that Novation and Premier's true purpose in the marketplace as GPOs is "to deliver substantial market share to monopolistic medical device manufacturers, such as Becton Dickinson and Tyco, in exchange for substantial 'administrative fees' and other forms of remuneration." Further, the complaint stated, GPOs require member hospitals to purchase as much as 90 percent of their supplies from their contracted vendors, with incentives for even higher levels of compliance, thereby blocking out small manufacturers.

The defendants denied any wrong-doing, but Novation, Premier, and Tyco all settled with Retractable in April 2003 for an undisclosed amount plus promises to allow Retractable access to hospitals. Shaw said that Becton Dickinson, the lone remaining defendant, settled in July 2004 for \$100 million.

When asked for comment, Gentry, the Novation spokesman, requested that the Weekly submit written questions via e-mail. Most of the questions posed to Novation went unanswered, however. The spokesman did say that news coverage of the company has been "rife with errors" and that Novation has had to spend a lot of time "educating the media" and trying to repair "the damage caused by accusations from certain manufacturers" like Retractable.

As for Masimo, the company sued Tyco in 2002 but not the GPOs, although they were cited in the complaint as sharing an interest with Tyco in keeping Masimo out of hospitals through "anti-competitive agreements." Masimo also alleged that Novation's contract with Tyco gave larger discounts to hospitals that purchased at least 95 percent of their oximeters from Tyco. "The most favorable price discounts," the complaint stated, "are not linked to sales volume, but ... to the exclusion of competition." The complaint also alleged that Novation offered additional incentives to hospitals that purchased bundles of products from Tyco, leaving Masimo, which sold only oximeters, in an uncompetitive position while giving Tyco larger sales for many different supplies. A hospital that bought 95 percent of its supplies from a list of 12 Tyco product categories could receive a rebate for as much as 7 percent of its purchase.

Eventually pressure from doctors and nurses who clamored for Masimo's oximeter led Premier to grant Masimo a contract shortly after the lawsuit was filed. Novation did the same a year later, only days before its CEO was scheduled to testify before Congress. Masimo's revenues have taken off since it gained that access to hospitals, and the company now has revenues in excess of \$100 million a year. In March of this year, a jury concluded that Tyco owed Masimo \$140 million in damages. Tyco has appealed this verdict.

Other small manufacturers have followed in the footsteps of Masimo and Retractable Technologies, suing the GPOs to gain access to hospitals. Nick Patton, a lawyer in Texarkana, is representing Genico, a manufacturer of laparoscopic surgical equipment, and Rochester Medical, which makes catheters, in federal antitrust lawsuits against Novation, Premier, and Tyco.

“These companies’ products are competitive and represent a significant advance,” he said. “The bottom-line effect of GPOs’ practices is to cut out competition. It seems near impossible for a new company with a great product and good pricing to get in the marketplace.”

The floodgates may have been opened for small companies who want a piece of the GPOs. Patton said that he’s talked to two or three other companies about possible litigation against Novation.

With 2,400 hospitals as members, Novation controls access to close to a third of hospitals nationwide and claims to have saved its members \$1 billion in 2003. But the company does not release information on its revenue. In fact, Novation’s reputation is one of extreme secrecy.

“I’ve talked to member hospitals who say it’s like getting info out of the CIA,” said Rudikoff, of the medical workers union. “They’re not open at all with them. As far as outside community scrutiny, they don’t disclose anything to the public. They’re resistant to any kind of oversight. Novation is a private entity owned by hospitals, which are a public trust, but they act as though everything is their own private business, which just happens to be 60 percent sponsored by taxpayers.”

Many in the industry suspect Novation’s earnings go far beyond the 3 percent of sales that Congress envisioned. Novation itself admitted that 30 percent of its contracts exceeded that, although following congressional hearings, the company said it voluntarily capped its fees at 3 percent, and Gentry, the Novation spokesperson, told the Weekly that the average fee is now 2.1 percent. Fees in excess of 3 percent of sales are supposed to be scrutinized for possible abuse by the Centers for Medicare and Medicaid Services.

After Senate subcommittee hearings last year on GPOs’ influence on the healthcare market, legislation was proposed by U. S. Sens. Herb Kohl of Wisconsin and Mike DeWine of Ohio that would have more strictly regulated the purchasing groups, but the bill never made it out of committee. More hearings are scheduled for next year — and a Senate Judiciary Committee source said the GPOs’ self-imposed code of conduct as well as the “safe harbor” provision will be under scrutiny. “There’s also a valid concern that the GPOs are getting bigger and bigger,” the source said. The high rate of consolidation in the industry, he said, “makes this an antitrust issue.”

At the end of each year, Novation’s earnings beyond operating expenses technically are supposed to go back to their member hospitals — but that doesn’t always happen. GPOs can use administrative fees to finance other ventures. In Novation’s case, it invested heavily in a struggling company in a deal that left industry experts scratching their heads.

Neoforma was one of the darlings of the dot-com bubble. Started in 1996 to enable hospitals to order supplies through the internet, Neoforma was embraced by Wall Street, and its stock reached a price of \$735 shortly after it went public in 2000. After that, it was all downhill for the company. As investors realized that the company’s earnings prospects were miserable, the stock price plummeted, reaching \$5.66 at one point after a stock split. But where market watchers saw little hope, Novation saw an opportunity. In 2000, Novation invested its member hospitals’ money in a deal that made Neoforma into Novation’s e-commerce partner for 10 years. UHC and VHA, the two hospital consortia that formed Novation, came to own 50 percent of a company that has bled more than \$700 million in red ink since it came into existence.

Neoforma’s main source of revenue came from that business relationship it formed with Novation. Neoforma had \$74.4 million in revenue in 2004 — mostly from suppliers that were forced by their agreements with Novation to also sign up for Neoforma’s e-commerce service. But Neoforma also reported losses of \$61 million. Some member hospitals, according to The New York Times, complained about Novation’s investment in a hopeless company.

Some Novation executives also owned shares of Neoforma — which hospital officials pointed to as a conflict of interest. Curt Nonomaque, chief executive officer of VHA and a board member of Novation, had personally invested \$150,000 in Neoforma, although he sold that stock in 2001. When congressional pressures for reform caused GPOs to institute an informal code of conduct, GPO board members had to declare conflicts of interest, including investments in companies that did business with the GPOs. This resulted in several board members at Novation leaving the company rather than selling their stock.

And Neoforma didn't just hemorrhage money — it infuriated suppliers who alleged that forcing them to pay for Neoforma's service was a double-dip by Novation.

“Neoforma has generated so many losses it's just been a huge albatross around Novation's neck,” said a medical supply chain expert who did not want to be named because, he said, GPOs have “destroyed his life” for comments he made in the past. “Novation was Neoforma's largest consumer — that's the revenue that's been keeping Neoforma afloat. If they lost that, they would disappear. People at VHA and UHC didn't look real smart taking their members' money and investing into Neoforma.”

Mark Lahey, executive director of the Medical Device Manufacturers Association, a group that represents small manufacturers like Retractable and Masimo, said Neoforma's business model made little sense for Novation to invest in.

Lahey said that Novation insists its vendors sign up for Marketplace@Neoforma, which “charg[es] six figures for companies to list their products with Neoforma. And Novation pimps them endlessly, even though they're losing money.” Unfortunately, he added, “Hospitals aren't looking as closely as they should” into what Novation does with their money.

The latest developments regarding Neoforma have been even stranger. Last month, Neoforma announced a merger with Global Healthcare Exchange, its only remaining competitor in healthcare e-commerce. The action came after Neoforma's gloomy prospects forced it to consider a merger “to achieve maximum shareholder value” — and, reportedly, to stave off bankruptcy. In the pending merger, individual Neoforma stockholders would receive \$10 a share — while VHA and UHC would end up with major ownership positions in the new company.

GHX is a privately owned enterprise belonging to Premier and 80 of the largest medical supply manufacturers, including Becton Dickinson and Tyco. The merger means Novation has jumped in bed with its largest rival.

“This is just another opportunity for Novation and Premier to get together along with all the large manufacturers and have meetings behind closed doors,” said the supply chain expert. “By having GHX come and buy Neoforma, Novation executives look like geniuses to their member hospitals, although they're really creating a monopoly. The GPOs are supposed to be fighting the manufacturers, but instead they're openly getting in business with them.”

The deal may or may not make Novation execs look good in the long run. Neoforma is facing a class-action lawsuit in Delaware filed by shareholders who allege that the deal is unfair to them. Lawyers for the shareholders declined to comment on the case.

If people like Shaw, Patton, and Lahey sound paranoid about a conspiracy involving hospitals, big manufacturers, and GPOs combining to rip off American healthcare consumers, they're not alone. Medical Supply Chain, a Missouri company that develops software that enables hospitals to order supplies directly from manufacturers, alleges that Novation and Neoforma, in conspiracy with manufacturers, distributors, and suppliers, have charged \$100 billion in excess costs to hospitals since 2002. The anti-trust lawsuit seeks \$1.5 billion in damages from Novation, Neoforma, and their executives, as well as US Bank and investment firm Piper Jaffray.

Samuel Lipari, CEO of the Missouri firm, said that his company's troubles began in 2002. Lipari sought funding from US Bank to start MSC. The loan, which seemed like a sure thing, was denied. US Bank cited a money laundering provision of the USA PATRIOT Act as the reason, telling Lipari that his company “could not really give all the correct answers on the source and flow of money” for Medical Supply Chain. Lipari and his attorney, Bret Landrith, argued that the PATRIOT Act seemed irrelevant to a company in good standing with the state of Missouri and clearly traceable funds from U.S. citizens seeking a bank loan.

“We knew Medical Supply Chain could save hospitals 40 percent over the prices they pay,” said Landrith. “Web-based exchanges like ours can make hospitals more efficient than Wal-Mart.” But as they looked into the problem, Landrith and Lipari said they noticed that US Bank had a business relationship with Piper Jaffray, which in turn had a relationship with Novation and Neoforma. The only explanation for denying funding to MSC, which claims that it could save hospitals \$80 billion, was that Piper Jaffray, US Bank, and Novation

conspired to keep MSC out of the marketplace.

“They’re keeping us out of the market,” said Lipari. “There’s a vast number of other companies with technology to improve healthcare that Novation’s monopoly is doing this to. Our litigation is identical to Retractable’s, and the evidence is parallel to their case.”

An independent study by Harvard Law School Prof. Einer Elhauge brought together all the arguments against GPOs. He said that contracts requiring hospitals to purchase 90 percent or more of their supplies from large vendors exclude rivals and harm consumers and hospitals to the tune of \$6 billion a year. The loyalty rebates, he said, act as penalties for hospitals that stray from the GPO. Beyond that, Elhauge concluded, the GPO process also stifles the development of even more innovative products.

The Justice Department is taking Novation’s role in the market seriously. In August of last year, shortly before the Senate subcommittee held hearings on tighter regulation for GPOs, federal prosecutors in Dallas opened a criminal investigation into the medical supply industry, with Novation at the center of it.

Federal officials declined to comment on the investigation, which came to light when Becton Dickinson revealed in its financial statements that Justice had issued subpoenas regarding its transactions with Novation. Officials at Novation also confirmed receiving federal subpoenas demanding documents, but pointed out that investigations could be launched without evidence of misconduct.

Based on the subpoenas, the investigation appears to be seeking evidence of Medicare fraud and conspiracy to defraud the United States.

“Hospitals get a big fat check once or twice a year from the GPOs,” explained one expert who is close to the investigation. “No other deal gives free money to a hospital. And they can report checks not as a reduction in cost, but as miscellaneous income. This allows them to be reimbursed ... for the original price before they account for the money they get from GPOs and manufacturers. That’s what the investigation is about.”

The huge volume of documents that investigators are having to sort through has dragged the process out for more than a year, another source said, and pointed out that hospitals and manufacturers have received subpoenas as well as GPOs.

The investigation wasn’t helped when two federal prosecutors involved in the case died weeks apart from each other. Thelma Colbert, who headed a civil litigation unit of the Fort Worth DOJ office that prosecuted companies involved in defrauding government-funded programs, drowned in her swimming pool in July 2004. The Tarrant County medical examiner’s office determined the death was accidental. Then, on Sept. 13, 2004, Shannon Ross, the criminal chief for the U.S. Attorney’s office in Dallas, who reportedly had signed the GPO subpoenas, was found dead in her Rowlett home. In that case, the Dallas County medical examiner ruled the death to have been from natural causes.

About the same time federal prosecutors were launching their investigation of Novation, the company also came under scrutiny from Connecticut Attorney General Richard Blumenthal, whose office, he said, was “very interested in potential undue influence exerted by vendors and manufacturers on individuals in positions to make healthcare purchasing decisions.” No indictments have been returned in either the state or federal investigation, but Blumenthal’s office is continuing to serve subpoenas.

Gentry, the Novation spokesman to whom the Weekly delivered its written questions, was also asked to arrange interviews with company officials regarding the investigations. The spokesman said executives did not respond when he mentioned the Weekly’s requests. He also said no company executives were under government investigation.

Meanwhile, Mark McKenna, CEO of Novation, announced his intent to step down in spring of 2006, after his successor has been appointed. The press release announcing this did not give a reason for McKenna’s decision, but the spokesperson said McKenna, who is 56, “wants to enjoy life.”

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