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Reducing the Subsidization of Employed Physicians

Hospitals and health systems allocate a tremendous amount of time, money, and effort to develop and manage employed physician networks. In almost all cases, networks owned by hospitals lose money on direct revenue versus expenses, but generate a positive margin on downstream referrals. Given the financial challenges facing the health care industry and the economic crisis in the United States, now more than ever, physician and overall financial subsidies in physician networks must be managed at reasonable and appropriate levels.



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"Physician Employment:
A Win for Providers
and Physicians"

About one-quarter to one-third of physicians in the United States are employed by a hospital or health system. This percentage is projected to increase for the foreseeable future. Surveys indicate that more than 50 percent of physicians completing training programs will strongly consider employment rather than a private practice option.

Why Employment is an Attractive Option

A variety of factors are driving the increased number of employed physicians. Ask senior hospital executives, and they'll tell you that for

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them, physician employment

- Enhances access to physicians and is an effective recruitment vehicle
- Protects and bolsters the referral base
- Mitigates the call coverage challenge
- Fosters a collaborative rather than a competitive relationship with physicians
- Improves physician-hospital alignment through shared information systems and other means of clinical integration
- Increases bargaining power with payors
- Generates referrals and downstream revenue

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Does the Primary Care
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Change?"

Physicians are likely to report that employment arrangements offer them

- Security
- A balance between their home and work life
- Less financial risk than private practice
- An opportunity to increase compensation
- A better overall fit if they possess less entrepreneurial spirit than the previous generation of physicians

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"When Should You
Consider Acquisition?"

Financial Implications of Employment

In the mid-1990s, when hospital employment of physicians materialized at a frenzied pace, networks often lost in excess of \$100,000 annually per FTE employed physician. Following hard lessons learned over the past 15 years, hospitals are now more skilled at structuring employment agreements with incentives to motivate employed physicians. These incentives typically include productivity-based compensation, as well as targets for physicians to improve efficiency, patient satisfaction, and quality. In most cases, practices consisting of hospital-employed physicians still offer less in the way of ancillary services than peers in independent physician practices because these services often compete with existing hospital ancillary services. The absence of these services limits revenue potential and ultimately diminishes overall financial performance.

The Medical Group Management Association (MGMA) survey results show an increase in the operating subsidy per FTE employed physician to more than \$85,000 in 2007, after ranging from \$65,000 to \$70,000 in each of the past several years. Practice managers attribute the increased subsidy to a more challenging economy, an increase in the number of uninsured patients, and higher losses per FTE for new or recently employed physicians.

MGMA Integrated Delivery System Net Income, Excluding Financial Support (All Practices) Per FTE Physician, 2005-2007				
	2005	2006	2007	Percent Change 2005-2007
Median Support	\$67,901	\$68,881	\$86,181	26.9%

Source data obtained from:
MGMA Cost Survey Reports (Based on Previous Year's Data), 2006, 2007, 2008.

Improving Network Performance

When hospitals evaluate their employed physician network, they usually decide to maintain or grow the employed network to provide a stable base of physicians with whom to work, increase opportunities for alignment, and solidify their referral base. But as history has shown, employment comes with costs—often high costs. What can health care organizations do to gain the multiple benefits of physician employment and offset the financial risk? To enhance the future viability of employed physician networks, hospitals should:

- Carefully select employed physicians and structure employment contracts with explicit language regarding the expectations and productivity incentives for physicians
- Provide regular feedback and data to employed physicians on productivity, quality measures, revenue generation, expense levels, overall operations, and other measures of practice performance
- Establish guidelines for the per-physician operating loss or subsidy that will be tolerated
- Structure employment relationships for a limited term (one to three years) so that each party can assess the appropriateness of the employment relationship
- Assign management of the physician practices to experienced professionals who understand the practice operating environment
- Give the employed physician network and other formal physician-hospital relationships the high-priority attention they deserve; for example, assign oversight of the network to a member of the senior management team
- Avoid excessive allocation of overhead expenses to physician practices
- Manage larger administrative functions like billing and collections, allowing physicians to handle day-to-day operations of their practice
- Continuously evaluate employment relationships to identify if changes in reimbursement, the regulatory environment, or competitor initiatives warrant a change in the structure or terms

of the relationship

Key Characteristics of a NJ Health System's Employed Physician Network

A New Jersey-based health system has been growing its employed physician network over the past five years and now employs approximately 50 physicians; almost 95 percent are primary care providers. The health system estimates that when downstream revenue and other benefits are quantified the overall contribution margin to the system is positive by more than \$5 million. In 2008, the health system subsidized the network by about \$4 million overall, approximately \$80K per employed physician. As part of an initiative to reduce the per physician subsidy by 10% (for returning physicians), each employed physician in the network now has performance incentives based on quality and productivity.

The health system realizes multiple benefits from the employed network including a strong referral base for affiliated specialists and existing and new programs. The network has enhanced access to physicians for residents of the services area, particularly Medicaid and uninsured populations, and has decompressed use of local emergency departments. Employed practices located on the periphery of the system's service area serve as competitive outposts for the system. Greater collegiality and improved communication among physicians has been fostered by the network, which now serves as a forum for the physicians to share data on length of stay and resource utilization so that they can ultimately improve care provided to their patients.

When organized and managed well, employed physician networks can be one of a cadre of initiatives that form the foundation of strong and healthy physician-hospital relationships. But providers must be vigilant to ensure that the benefits justify the expected losses.

For more information on employed physician networks, please contact [Robert Hill](#) at 215-399-1856 or [Craig Holm](#) at 215-399-1899.




Robert Hill



Craig Holm


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