

Insight Health Partners White Paper: CLEAR AND PRESENT DANGER: Understanding the Issues that will Complicate Physician Compensation Plans (and the Bottom Line) in 2021

Managing compensation plans for health system employed physicians has never been an easy task for obvious reasons. After a challenging 2020, where health system leaders were faced with a once in a lifetime event, discussing hidden and potentially silent threats to physician compensation plans and bottom-line performance may seem like cruel and unusual punishment. However, given that threats are already in play as of January 1, 2021, now is the appropriate time to understand key issues and develop mitigation strategies to avoid having to make more difficult decisions down the road.

Why does this matter? There are multiple issues that threaten to significantly impact the compensation of a health system's highest paid employees in 2021, 2022 and possibly beyond. Potential negative outcomes for health systems and their employed physicians could include some or all of the following:

1. **Cost increases.** Physician compensation costs for primary care physicians may increase significantly on an annual basis in 2021, 2022 and 2023. Assuming primary care physician capacity and productivity are unchanged from 2020 levels, compensation costs could increase by more than 10 percent a year over the next 2 years.
2. **Group practice performance deterioration.** Unanticipated (and possibly unbudgeted) increases in group practice operating losses are projected unless a thoughtful approach is developed to avoid/minimize key issues. Deteriorating performance will be caused by unexpected physician compensation expenses coupled with a lack of offsetting professional services revenues.
3. **Agitated physicians.** It is almost inevitable that the national survey data will see a substantial increase in variation versus surveys from prior years. This will cause a high level of frustration with administrative leadership and physicians as they attempt to interpret the data. In many cases the questions raised by physicians related to the reliability of the market data will be valid. Any solutions developed and implemented by management will also be subject to increased scrutiny and require considerable physician socialization and education.

What are the threats? There are two factors that are about to throw a monkey wrench into the national survey data that will be impacting physician compensation rates and group practice performance for the next two and possibly three years before a steady state is finally achieved.

The COVID Effect

Insight has surveyed multiple clients regarding their approaches to physician compensation during 2020 given the impact of COVID. Given a sizeable reduction in physician patient volumes and associated work relative value units (wRVUs), health systems generally pursued one or more of the following strategies:

1. Temporarily freeze physician compensation at past levels despite substantive drops in wRVUs associated with reduced patient volumes/clinic closures as health care leaders grappled with how to manage through the pandemic in early/mid 2020.
2. Reduce physician compensation levels consistent with salary cuts implemented throughout the remainder of the organization, i.e., shared pain.
3. Status quo, i.e., continue to manage the physician compensation plan and calculate payments and bonuses with no changes in rates or procedures. Given that a large majority of compensation plans are heavily weighted toward productivity, this option would have eventually led to material compensation decreases in 2020 with the exception of physicians on salary guarantees.
4. Physician capacity “right-sizing”. To the extent that health systems may have already been contemplating physician FTE reductions, COVID-19 provided the burning platform to move forward with implementation.

The COVID Effect will be reflected in the 2020 data that was provided to the major survey companies and will be released in mid to late 2021 as part of the 2021 Physician Compensation Surveys (based on 2020 data). While the COVID news appears to be trending more positive in 2021 coupled with healthcare providers being more educated on how to safely operate, the COVID Effect on provider productivity will continue to significantly impact 2021 data and thereby will also be reflected in the 2022 national surveys. Mid to late 2023 may be the first time when the national physician compensation sources are truly “COVID free”.

The Medicare 2021 Physician Fee Schedule (PFS) Effect

Let’s start with a very brief history lesson. Over the past 12-13 years, CMS has typically implemented incremental changes to the Medicare Physician Fee Schedule (PFS) on an annual basis. Changes usually include some CPT code updates as well as RVU weight changes implemented on a budget neutral (or close to budget neutral) basis. Unfortunately, this was not the approach that CMS took with the 2021 Medicare PFS, which deviated substantially from prior years. For those that remember, the 2021 PFS somewhat resembles the curve ball that CMS threw at us back in 2007/2008. Key changes introduced on January 1, 2021 include:

- *Fundamental (and significant) changes in RVU weights.* Unlike prior years, the 2021 re-weighting was not completed on a budget neutral basis and they will impact physicians differently depending on specialty. Specialties that are heavily dependent on E&M (Evaluation & Management) codes (like primary care and psychiatry) will see their wRVUs jump significantly in 2021 for the same work they did in 2020. These also tend to be specialties that comprise a high percentage of the physicians in health system aligned physician groups. For one Insight client, the net impact of the 2021 Medicare PFS is a projected additional operating loss for family medicine of \$75K per physician FTE. This operating loss will occur in addition to historical losses, which are already substantive.
- *A conversion factor (CF) reduction of approximately 4%.* This is how Medicare offset what would have been the sizable cost increase caused by RVU re-weighting. Unfortunately, it also means that Medicare does not fully fund the RVU change. For primary care, the increased physician compensation cost of pure wRVU production compensation model will not be offset by increased revenue.

How will the 2021 Medicare PFS impact physician compensation surveys? Time will tell and it's a bit of an educated guess. To some extent, it will depend on the data that providers submit in 2022, which will most likely vary widely across health systems. It will also depend on the compensation plans utilized by health systems. In case study outlined below, two physicians generate the same wRVUs and are compensated the same amount in Year One (2020). The only difference between Physician A and Physician B is their compensation plan. Physician A is compensated using a guaranteed salary while Physician B is compensated using a production model based on wRVUs. It is also assumed that the physicians' health system employers utilize RVU weights as defined by Medicare for each year, i.e., the health systems calculate wRVUs based on the RVU weights defined in the Medicare PFS on January 1 of each year. Both physicians also bill the same volume and mix of CPT codes in 2020 and 2021.

Family Medicine Physician A Compensation Model: SALARY GUARANTEE	Family Medicine Physician B Compensation Model: 100% PRODUCTION (wRVUs)
<ul style="list-style-type: none"> • Paid a guaranteed salary of \$250,000 in both 2020 and 2021. • Bills the same volume and mix of CPT codes in 2020 and 2021. • Calculated wRVUs increase from 5,000 in 2020 to 6,000 in 2021 for the same clinical work effort in both years. • Physician A's compensation per wRVU would decrease from \$50.00 in 2020 to \$41.67 in 2021. 	<ul style="list-style-type: none"> • Bills the same volume and mix of CPT codes in 2020 and 2021. • Calculated wRVUs increase from 5,000 in 2020 to 6,000 in 2021 for the same clinical work effort in both years. • Paid calculated compensation using a CF of \$50 of \$250,000 in 2020 and \$300,000 in 2021, <u>a 20% increase in cost with no change in clinical work effort.</u>

The year of year impact of the two compensation plans and the impact of the 2021 Medicare PFS RVU weights are summarized below:

Exhibit A: Side by Side Comparison of Family Medicine Case Study

	Family Medicine Physician A Compensation Plan: Salary Guarantee				Family Medicine Physician B Compensation Plan: Production Model			
	Year		1 Year Percent		Year		1 Year Percent	
	2020	2021	Change	Change	2020	2021	Change	Change
wRVUs	5,000	6,000	1,000	20%	5,000	6,000	1,000	20%
Compensation	\$250,000	\$250,000	\$ -	0%	\$250,000	\$300,000	\$50,000	20%
Compensation/wRVU	\$ 50.00	\$ 41.67	\$(8.33)	-17%	\$ 50.00	\$ 50.00	\$ -	0%

How will the 2021 physician compensation surveys be impacted?

So what is likely to be reflected in the 2022 Compensation Surveys (based on 2021 data)? There are a wide range of possibilities and it will depend on what gets dropped in the *data blender* and summarized in future surveys:

- Possibility A: Data reported for 2020 (to be utilized in the 2021 surveys) reflects large decreases in physician wRVU production (caused by COVID-19) while compensation levels may remain flat or show slight decreases from 2019 reported data. While compensation may show a decrease on a per FTE basis, it is very possible that there will be a significant increase in calculated compensation per wRVU for E&M-based specialties including primary care which could be reflected in surveys published in 2021.
- Possibility B: Many organizations compensate their primary care physicians in 2021 using the 2021 RVU weights and survey CFs **that are based on 2020 RVU weights**. The net effect could be a considerable increase in primary care physician compensation costs in 2021 with no actual increase in physician production. This artificial and significant increase in physician compensation could first present itself in the 2022 Physician compensation surveys, although the increased physician compensation cost will show up much earlier in the income statements for the group practices.
- Possibility C: Organizations continue to use 2020 RVU weights for physician compensation calculations in 2021 (a very reasonable short-term solution). When those same health systems provide 2021 RVU data to the survey companies, will it be based on 2020 weights (used to calculate physician compensation) or 2021 weights (the values used by Medicare for reimbursement purposes)? It will most likely be a hodgepodge of both.

Insight has summarized the potential threats to physician compensation and how the impact will most likely be felt by health systems on an annual basis in Exhibit B below.

**Exhibit B: What and When?
Projected Timing and Impact of Key Physician Compensation Issues**

	2021	2022	2023
The COVID Effect	<ul style="list-style-type: none"> • The first year that national compensation surveys reflect COVID impacted data. • High probability that CFs for many specialties increase by +5% as a result of COVID impact. 	<ul style="list-style-type: none"> • COVID continues to significantly impact data and survey results. 	<ul style="list-style-type: none"> • Most likely the first “COVID-free” survey since 2020 (the 2020 surveys are based on 2019 or pre-COVID data).
The 2021 Medicare PFS Effect	<ul style="list-style-type: none"> • 2021 Medicare PFS goes live January 1. • Some (not all) health systems freeze RVU weights at 2020 levels for physician compensation calculations. • Primary care physician compensation costs unintentionally spike for physician groups using 2020 CFs and 2021 RVU weights. 	<ul style="list-style-type: none"> • The first year that national compensation surveys reflect 2021 Medicare RVU weights. • 2022 surveys should (in theory) reflect new RVU weights. • High probability that a significant number of survey participants provide 2021 wRVUs data based on 2020 RVU weights. 	<ul style="list-style-type: none"> • High probability that 2023 is the first year that reported CFs are actually based on RVU values using the new RVU weights, i.e., post 2020 weights.

Final Thoughts

If the current threats impacting physician compensation have a déjà vu feel to them, it is because the Medicare PFS changes are somewhat similar to what occurred in 2007. This was when many health care organizations were caught flat-footed and ended up absorbing many physician compensation cost increases that were not supported by increased clinical work effort or professional revenues. 2021 feels eerily similar, but with the added complexity of COVID-19.

What should happen? Health care leaders should evaluate some or all of the following strategies:

- Continue to calculate provider wRVUs using CMS' 2020 weights until such time that leadership is confident that national survey data reflects the impact of the RVU re-weighting that occurred on January 1, 2021.
- 2021 Physician Compensation surveys should be handled with care and come with a warning label. Carefully evaluate the accuracy and risk associated with the 2021 physician compensation surveys. Determine whether a better approach will be to continue to utilize 2020 surveys (possibly with inflation adjustments) until such time that leadership is confident that data has reached a steady state.
- Complete a significant amount of provider education on issues impacting physician compensation and the mitigation plan to bridge from now through 2023.

What will happen? Time will tell what actually transpires in 2021 and 2022. Fortunately (or unfortunately) the post mortem story will be told in physician group operating performance and the trended survey data from 2020 to 2023 which will be impacted by the quality of data provided.

For more information, contact Craig Pederson or Brett Turner at Insight Health Partners:

Craig Pederson cpederson@insighthp.com 612.817.1232	Brett Turner bturner@insighthp.com 847.340.0368
---	---