

# Medical Liability Watch

exploring the business side of medicine



Though many professionals have experienced an increase in annual income during the past decade, physicians and other healthcare providers have found themselves struggling to make ends meet. This article examines some of the factors that contribute to physicians' financial pressures and provides practical suggestions for remaining financially viable in today's complex healthcare environment.

## strapped

a look at the **financial** challenges  
of practicing **medicine**

By Katherine Cleghorn,  
*Communications Specialist*

Since the mid-1990s, physicians' annual incomes have declined steadily. According to researchers at the Center for Studying Health System Change, "between 1995 and 2003, average physician net income from the practice of medicine declined about 7 percent."<sup>1</sup>

Although many factors have contributed to the drop in physician incomes over the past decade, three trends in particular appear to be the primary drivers: the nationwide growth in managed care, cuts in public program payments to physicians and the rise in practice costs brought about by the increase in medical malpractice suits.

Managed care, which became widely adopted in the late 1980s, was designed to help improve patient safety and stem the rising costs of healthcare. Unfortunately, managed care also contributed

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to significant decreases in physician compensation as a result of capitation. Capitation payments are fixed amounts that are paid to physicians and hospitals in advance of the services they will provide patients. Many experts believe this fixed payment structure is inherently flawed, as it does not take into account the amount or type of services that will be provided to patients and the costs these services incur. Capitation also shifts financial risk from the insurance company to the provider. Since the expenses for treating patients come from one common pot, providers are often forced to take a loss if there is no money left over after expenses have been covered.<sup>2</sup>

Declining fees from public programs such as Medicare and Medicaid, particularly Medicare's drastic rate reduction in 2002, have further threatened physicians' financial health. During the past decade, the few rate increases that have been instituted by Medicare have been negligible because they lagged substantially behind inflation rates.<sup>1</sup> The situation may worsen if additional cuts proposed by the federal government are enacted in 2007.

Physicians must also deal with the fiscal ramifications of the current medical malpractice litigation climate. Despite the success of medical tort reform initiatives such as California's Medical Injury Compensation Reform Act (MICRA), the frequency and severity of malpractice suits continues to be a problem.<sup>3</sup> The current malpractice environment affects physician incomes on a variety of levels, influencing everything from malpractice insurance premiums to the amount of time a physician must spend away from work if he or she must defend a claim.

The ever-changing healthcare climate is yet another factor contributing to physicians' financial pressures. Many physicians cite high overhead as one of their most pressing problems, particularly the prohibitive cost of hiring and maintaining a staff to manage daily operations. According to one study, 60 percent of physicians surveyed reported

that they spend between 40 and 70 percent of their revenue on overhead alone.<sup>4</sup>

Add to this the fact that as the healthcare climate has changed, so too have consumer attitudes. The high cost of American healthcare has an impact on the consumer as well as the physician, leading many consumers to seek more affordable ways to access care. More and more healthcare consumers are seeing healthcare extenders (HCEs), visiting the ER, or seeking out alternative medicine practitioners in an attempt to minimize the drain on their own wallets. As consumers seek alternative healthcare options, many physicians, especially primary care doctors and other generalists, find themselves in a position where they must compete with more aggressive, better funded providers for insured patients.

### **Grasping at Solutions**

Because more and more physicians are forced to compete for insured patients, some have begun to avoid treating low-income and/or uninsured patients altogether. Others are increasing their patients' fees, refusing to take call in hospital EDs (emergency departments) or demanding extra pay from hospitals for taking call.<sup>5</sup> Some physicians are even declining to participate in the Medicare and Medicaid programs due to low reimbursement rates, leaving many elderly and disabled patients with limited healthcare options.<sup>6</sup>

Conversely, some physicians have attempted to enhance revenue by taking on greater patient loads, increasing the volume and prices of services, investing in ancillary services and/or marketing products directly to consumers. Though these strategies have in many cases proven to be effective revenue generators, they can also be problematic. Larger patient loads often equate to less time spent with each individual patient and can lead to patient dissatisfaction. Investing in nontraditional services can be profitable, but only if the physician or practice can afford the initial capital outlay and additional staff that is required.

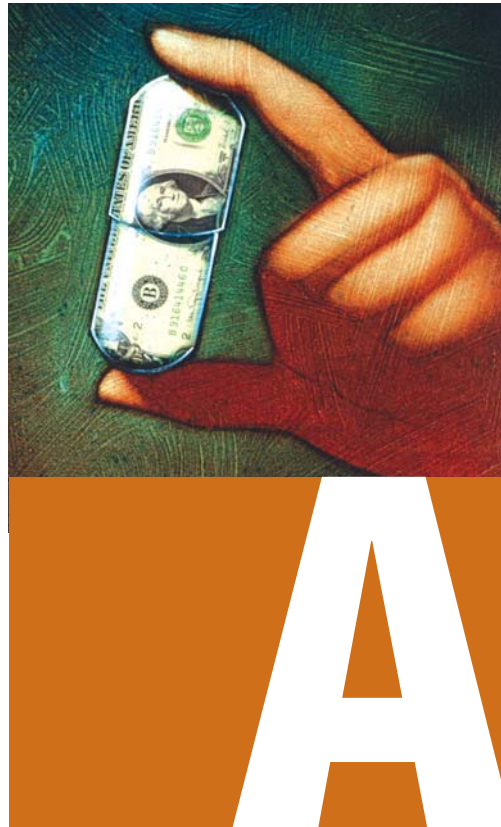
Some physicians are choosing to grow their businesses by offering their patients boutique services such as cosmetic surgeries, nutritional supplements and pharmaceuticals. These services can be profitable because they are not typically constrained by insurers' fee schedules, but many physician communities believe they can pose serious ethical issues, particularly when "therapies of questionable clinical value" are being offered.<sup>7</sup> In addition, if physicians do not take the time to train themselves and their HCEs regarding the proper administration of these products and services, poor patient outcomes can occur, leading to increased liability exposure.<sup>8</sup>

Clearly, today's physicians need a wider variety of solutions to help them deal with the financial challenges they're facing—solutions that are less likely to jeopardize the standard of care, pose liability concerns or put them at even greater financial risk.

### Experts' Suggested Remedies

Healthcare researchers have proposed a number of solutions to physicians' escalating revenue crisis, ranging from the personal to the institutional, the simple to the complex. Many experts suggest that financially strapped physicians can begin to improve the bottom line by simply taking the time to write business plans and develop budgets. According to healthcare consultant Paul Angotti, a well-thought-out budget can be the key to maintaining a financially sound practice. "Think of your practice's budget as a mini business plan covering this year and next," counsels Angotti. "This helps you establish a plan and adds a level of discipline to operations and spending."<sup>9</sup>

Physicians may also improve practice finances by examining ways to cut basic operating costs. Experts' suggestions include revisiting costly business contracts, addressing delinquent patient accounts, offering staff time off instead of cash bonuses, cross-training staff to perform a variety of duties, and buying in bulk rather than retail.



**As consumers seek alternative healthcare options, many physicians must compete with more aggressive, better funded providers for insured patients.**

These measures can be helpful in improving the financial outlook for some, but for many physicians more drastic changes are needed. A growing number of physicians are opting to join larger medical groups, where enormous overhead costs are alleviated by sharing the burden with peers. Experts also say that group practices are more equipped than most solo practices to gain valuable negotiating leverage with health plans.<sup>10</sup>

The nascent "pay-for-performance" movement, though controversial, has presented physicians with yet another option for increasing revenue. Pay for performance, or P4P, is a system wherein health plans pay bonus money to providers who meet certain benchmarks for patient care. P4P is rapidly gaining popularity among health plans and healthcare administrators, and has already begun to be instituted in certain states, including California.

Since the P4P concept is still in its early stages, however, it is unclear whether or not it will markedly improve physicians' revenues in the

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future. Because P4P is designed to incentivize physicians by offering them more money for providing better care, it's possible that players on all sides of the healthcare field could benefit: physicians, insurers, administrators and patients. On the other hand, P4P may cause some physicians to avoid or abandon difficult or time-intensive patients in order to improve overall scores. In addition, the IT infrastructure needed to obtain high scores is costly, meaning P4P tends to favor larger, wealthier providers and groups. Finally, there is currently no national standard for health plans to utilize when measuring quality medical care, and healthcare administrators and legislators are unclear as to when and how such guidelines will be set. Physicians should familiarize themselves with P4P's pros and cons and consider how the system may impact their practices, but should not rely on the P4P movement to drastically alter incomes.

### Choosing a Financially Sound Insurer

Experts believe that one of the best ways for physicians to get a handle on finances is by choosing a professional liability insurance carrier with a strong financial track record and solid industry standing.

Though affordable coverage is on everyone's mind these days, healthcare researchers counsel physicians to beware of insurers

whose premiums look too good to be true. "Numerous insurance companies have been placed into receivership and then liquidated over the last 10 years," say David Dearden and Michael Burke of the healthcare law firm Kalogredis, Sansweet, Dearden and Burke. "Many others have found professional liability insurance to be too problematic and no longer will underwrite such policies. Therefore, it is important to research the financial rating of your insurance company and those you are considering."<sup>11</sup>

Researching and choosing an insurance carrier can be complicated and time consuming, but in today's costly healthcare climate, the right insurer could make an enormous difference in helping to ensure a financially sound future for your practice.

Physicians face numerous challenges, and the financial constraints compounded during the last decade by managed care, public programs, the medical malpractice climate and other prevailing factors only intensify the difficulties doctors must deal with every day. Though there is no quick fix, options do exist that can help physicians remain viable in today's competitive healthcare market. Physicians can no longer afford to wait for policymakers to change the system—they must begin to take steps to ensure the future of their practices today.

### Endnotes

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# Supporting the Art of Medicine

## an interview with Dan Corrado

The editorial staff of *Medical Liability Watch* recently sat down with Dan Corrado, Vice President of Insurance Operations, to discuss NORCAL's physician-focused philosophy and commitment to supporting and protecting the art of medicine.

*NORCAL's business is built on a deep understanding of and appreciation for the practice of medicine.*

*Philosophically, how does this make the company different from other professional liability insurers?*

Because NORCAL is physician-owned, we are uniquely equipped to respond to our policyholders' changing needs. Unlike insurers that have more traditional corporate structures or are publicly-traded, NORCAL is not distracted by the pursuit of interests not central to our medicine-focused values, nor are we influenced by the vagaries of the healthcare and medical liability insurance markets.

Our policyholders are always our number one focus. We work to provide stability through adequate pricing and conservative rate making processes. We offer certain benefits not afforded by other insurers, such as policyholder dividends and the right to vote on Board members. We support early reporting of incidents and uphold the policyholder's full right to consent to settle a malpractice claim.

This year we've undertaken a major rebranding initiative to make sure that our policyholders, our employees and the marketplace know what we stand for: integrity, a passion for excellence and a profound commitment to the practice of good medicine.

*How do NORCAL's medicine-focused values drive the company's approach to customer service?*


There is a collaborative spirit at NORCAL that runs across all of our operational areas.

Though each department at NORCAL has a unique function, we all work together to achieve the same end goal of providing helpful services and superior protection to our policyholders.

Our Policyholder Services Unit is fully staffed with licensed insurance professionals who provide a direct point of contact for our policyholders' needs. We also offer cutting edge, clinically driven risk management programs to help policyholders enhance patient care while reducing their risk of malpractice claims.

In addition, we have physician Board members who work collaboratively to examine and evaluate clinical practices. Their combined medical expertise helps us develop guidelines that support our policyholders in their efforts to improve patient outcomes and mitigate professional liability risk.

*Arguably, NORCAL's primary function is to provide policyholders with peace of mind. How does the company accomplish this?*

Our policyholders can rest assured that we underwrite and defend claims based on the standard of care. We understand that a doctor's reputation means everything, and we will defend a claim to the end even if it is not the most economically advantageous approach for NORCAL. We also work hard to maintain our A.M. Best rating to ensure that we'll be here to defend policyholders in years to come. 

INTERVIEW





# MICRA PAC update

## California ASSEMBLY

|       |                       |      |
|-------|-----------------------|------|
| AD 06 | Cynthia Murray (D)    | LOST |
| AD 12 | Fiona Ma (D)          | WON  |
| AD 17 | Cathleen Gagliani (D) | WON  |
| AD 18 | Mary Hayashi (D)      | WON  |
| AD 21 | Ira Ruskin (D)        | WON  |
| AD 58 | Charles Calderon (D)  | WON  |
| AD 36 | Sharon Runner (R)     | WON  |
| AD 37 | Audra Strickland (R)  | WON  |
| AD 38 | Cameron Smyth (R)     | WON  |
| AD 69 | Claudia Alvarez (D)   | LOST |
| AD 75 | George Plescia (R)    | WON  |

## California SENATE

|       |                           |      |
|-------|---------------------------|------|
| SD 08 | Leland Yee (D)            | WON  |
| SD 10 | John Dutra (D)            | LOST |
| SD 20 | Alex Padilla (D)          | WON  |
| SD 28 | George Nakano (D)         | LOST |
| SD 32 | Gloria Negrete McLeod (D) | WON  |
| SD 34 | Lou Correa (D)            | WON  |

## June 2006 California Primary Election Results

NORCAL's MICRA PACs are focused exclusively on the issue of medical liability reform. To protect policyholders' interests and to make healthcare more readily available to patients, the MICRA PACs are playing a leadership role in the political process and ensuring that NORCAL policyholders' and other stakeholders' voices are heard.

One way we help shape the healthcare environment is to raise money through the PACs and contribute to legislators who support medical liability tort reform in California and in other states where NORCAL does business. The MICRA PACs have already made several solicitations of NORCAL policyholders, employees and key stakeholders in 2006. Through the first half of 2006, nearly \$50,000 was raised by the four MICRA PACs.

The most important task, however, is not simply raising money, but spending it wisely. This means we must build partnerships with legislators and candidates who truly support MICRA when the chips are down. The MICRA California PAC is pleased to report that we did in fact spend your contributions wisely in California's June primary election. The MICRA California PAC contributed to pro-MICRA primary candidates with victories in 13 of 17 races.

For the remainder of 2006 and in the coming years, NORCAL's MICRA PACs will continue to raise funds and spend the funds wisely on the behalf of our policyholders and MICRA's many supporters.

# Corporate Corner

## NORCAL Launches New Website

In September 2006, NORCAL launched our new corporate website, [www.norcalmutual.com](http://www.norcalmutual.com). The new site is designed to offer NORCAL policyholders and other stakeholders an enhanced online experience. Features of the new site include:

- More ways to get in touch with NORCAL
- More information about NORCAL's coverages, claims handling services, and risk management and CME programs
- Resources to support policyholders in their practices, including the *Claims Rx* and *Medical Liability Watch* newsletters and links to organized medicine



In addition to the main website, we've also revamped the secure My NORCAL Log-In section to make managing your account quicker and easier. My NORCAL Log-In users can make online bill payments, generate and send certificates of insurance (COIs) and credentialing letters, update contact information, view billing history and more.

Visit [www.norcalmutual.com](http://www.norcalmutual.com) today and discover all we have to offer. 🍷

## NORCAL Declares 2006 Policyholder Dividend

NORCAL recently declared a 2006 dividend for eligible policyholders in California, Alaska and Rhode Island. NORCAL policyholders and other stakeholders were notified of the dividend in late September.

The 2006 dividend, which will appear as a premium credit on billing statements for your 2007 policy term, applies to individual physicians and medical groups in California and Rhode Island and individual physicians, medical groups and hospitals in Alaska.

For eligible California and Rhode Island policyholders, the dividend will equate to approximately 6.75 percent of your prior year's premium. For eligible policyholders in Alaska, the dividend will equate to approximately 10 percent of your prior year's premium.

If you have any questions about the 2006 dividend, please contact NORCAL's Policyholder Services Unit at (877) 443-7232 and we will be happy to assist you. 🍷

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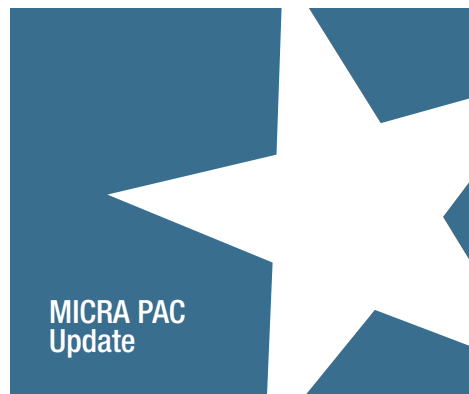
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# Inside . . .

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## Medical Liability Watch

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