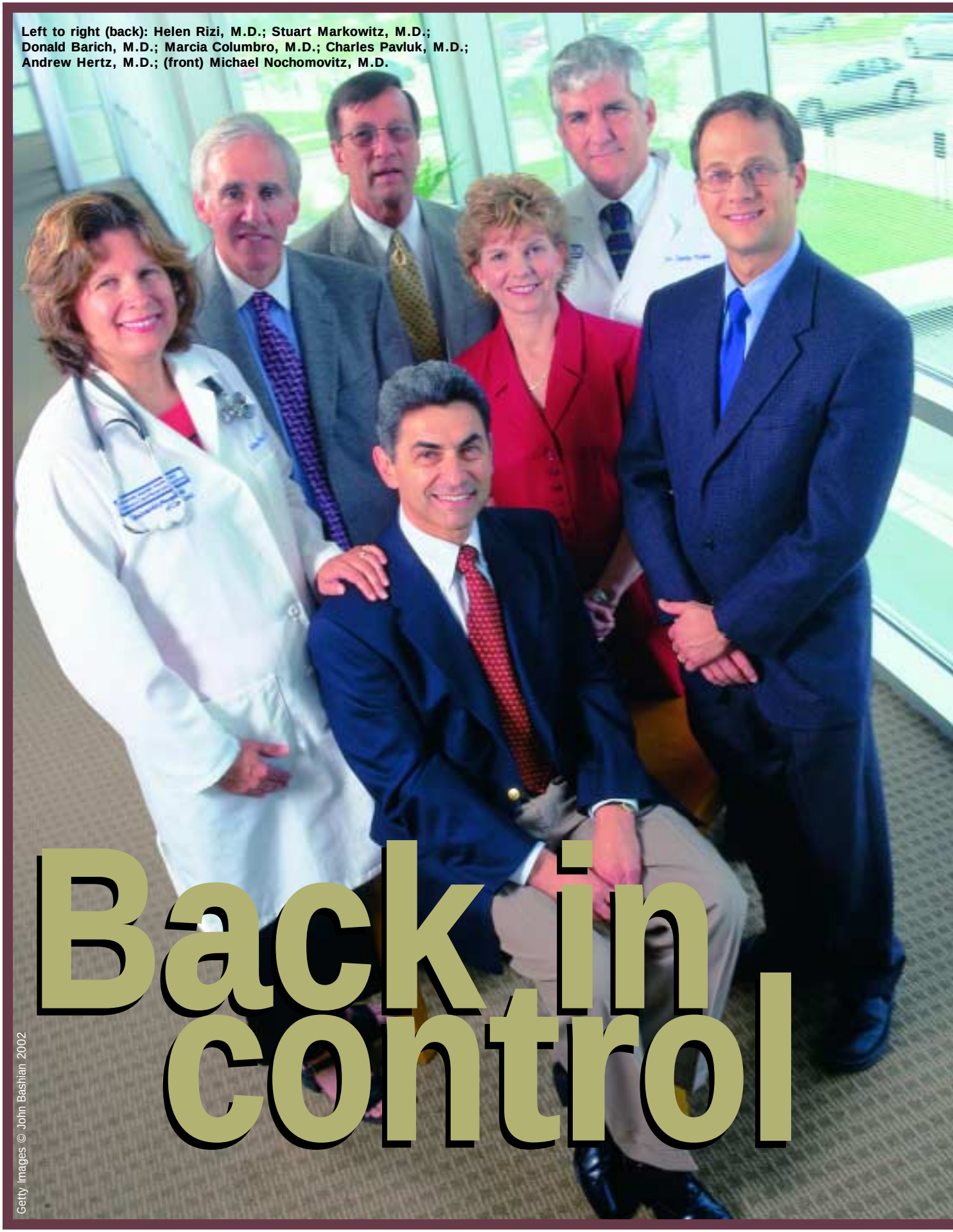


Left to right (back): Helen Rizi, M.D.; Stuart Markowitz, M.D.; Donald Barich, M.D.; Marcia Columbro, M.D.; Charles Pavluk, M.D.; Andrew Hertz, M.D.; (front) Michael Nochomovitz, M.D.

Back in control

Physician executives create new business models, picking salvageable ideas off the PPM scrap heap. by Neil Versel

AS a physician executive in academic medicine, Michael Nochomovitz, M.D., stood back as the physician practice management industry soared in the mid-1990s and crashed as the century turned.

He took what he learned from watching the arc of the PPMs when creating a new business model for University Hospital Management Services Organization and University Primary Care Physicians, both affiliates of Case Western Reserve University in Cleveland.

Nochomovitz, president and CMO of both organizations, and other physician leaders across the country are developing post-PPM management strategies that embrace the good from PPMs but reject the bad.

Some of the physician executives now cherry-picking ideas from the PPMs led their groups through both their sale to and repurchase from management companies.

One is Michael Redmond, M.D., a pediatric ophthalmologist and president of Medical Center Clinic, a 75-physician multi-specialty practice in Pensacola, Fla. In hindsight, Redmond says now, he sees it was a mistake to turn control of his practice over to another company.

"You can't expect other people to fix your problems. You have to fix them yourself," Redmond says.

Physician leaders and consultants say a major flaw of the PPM model was its failure to account for human nature—that physicians who were handed a fat wad of money for their practices and then put on salary wouldn't work as hard as they did when they were self-employed.

"If a doc was paid a lot of money for a practice and had a large nest egg put away, he loses the incentive to work 60 hours a week," especially if the physician is earning a guaranteed salary, explains Don Barbo, senior associate with Dallas-based medical practice valuation company Value Management Group.

"What it can create is almost like a downward spiral," Barbo says.

Fewer hours of operation meant a decline in patient revenue. But there were other problems, too.

"The PPMs failed because they tried to take community doctors away from the environment they belong in, both physically and culturally," Nochomovitz says. "An organization that wanted a long future couldn't stay in a model and in a culture that is artificial."

CASE STUDY

Nochomovitz's UPCP, a loose coalition of primary care practices, began in 1994, following the lead of the PPMs.

"We grew by acquisition in the same way everybody else grew," he says.

But by 1997, as the commercial PPM industry was peaking, something was wrong at UPCP, Nochomovitz says. Operating costs were too high, and revenues too low, in part because physicians had

Physician practice management companies make a comeback—sort of

The heyday of the large, publicly traded PPMs that owned hundreds of medical practices and employed thousands of physicians is long gone. But many of the firms are still around in one form or another.

Only a handful of single-specialty PPMs remain healthy. Pediatrix Medical Group (neonatal intensive care) and AmeriPath (pathology) are among the few with double-digit stock prices.

But many of the casualties of the PPM crash of the late 1990s have found a fresh start. The common thread in all the transformed PPMs is that none has direct control over physicians.

"It was more perceived control than real control," says Sharon De Rosa, COO of the Chicago Institute of Neurosurgery and Neuroresearch. "Once you have that middleman, it is perceived that way."

The practice is a client of NeuroSource, a Chicago-based subspecialty management firm that got out of practice management a year ago and now consults with about a dozen practices and health systems.

On July 31, Nashville, Tenn.-based PhyCor, the poster child of the meteoric rise and fall of the PPM business, emerged from bankruptcy protection as a privately held healthcare risk management company called Aveta Health. What remains is a 700-employee operation, down from a peak of 15,000, not counting the 4,200 physicians at PhyCor-owned practices.

Also in late July, Surgis, a surgical services company headed by former PhyCor chief Joseph Hutts, landed $100 million in venture capital commitments and closed on the acquisitions of an ambulatory surgical center operator and a firm that manages endoscopic services for hospitals. The new company does not own any practices.

MedPartners, once PhyCor's chief rival, sold its 85 Southern California practices to KPC Medical Management in August 1999 and restructured itself into Caremark Rx, a pharmacy benefits manager based in Birmingham, Ala. It also spun off Team Health, a Knoxville, Tenn.-based PPM for emergency medicine.

guaranteed salaries without incentives to produce additional revenue.

"We regrouped and decided to create a new contractual model for docs," he says.

They turned to the University Hospital MSO for management services and its business model. Nochomovitz describes the arrangement as an academic medical group with its own MSO but with decentralized authority.

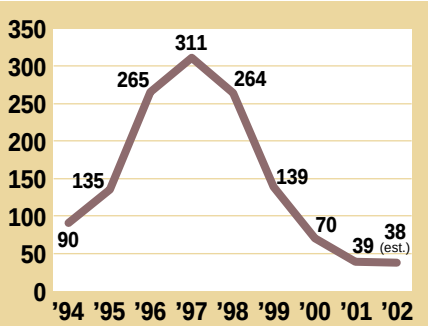
"It focuses on business processes, it focuses on quality of care and it focuses on customer satisfaction," he says. "We're more than an MSO. We are actively involved on the clinical side."

The reconfigured UPCP today includes about 230 physicians in 80 locations across 40 northeastern Ohio communities. Each practice is affiliated with the $2 billion University Hospitals Health System. It combines the financial muscle of a large organization with the autonomy of a private practice, according to Nochomovitz.

The MSO, a separate corporation that employs nonmedical physician office staff, acts as a facilitator by providing the groups with information, staff training and continuing medical education in best practices, including the use of technology for disease management, on a fee-for-service basis, Nochomovitz says.

The rise and fall of the PPMs

Physician practice mergers and acquisitions, 1994-2002*



* Includes purchases and sales by both management companies and physicians.

Source: Irving Levin Associates MP/Adam Doi

Like any private practice, UPCP groups earn money based on revenues minus expenses. But unlike others in an MSO-type arrangement, the physicians largely have financial autonomy.

"It's up to the doctors to decide how to divide up the money," Nochomovitz says. Mandatory risk management courses for all physicians helps the group negotiate lower malpractice insurance rates.

A recent addition to the UPCP network is Suburban Pediatrics, a six-physician practice with offices in Shaker Heights and Solon, Ohio. Medical Director Andrew Hertz, M.D., led a transition of the practice from a separate operating structure to a UPCP-owned practice at the beginning of 2002.

"We didn't think there was any advantage anymore being our own corporation," Hertz says.

One immediate benefit of joining UPCP was its pension plan administration. "We no longer have to pay a manager for our retirement fund," according to Hertz.

The model empowers physicians, he says. Even though everyone technically is employed by UPCP, the practice has the authority to hire and fire staff.

"We make all our own decisions as to how we want our practice to run."

He says Suburban Pediatrics has chosen to base compensation on productivity. There is no seniority, and the physicians split expenses and call responsibilities evenly.

OLD PROBLEMS STILL EXIST

Other groups, including those that sold to PPMs and later bought their way back out, still confront many of the same problems that pushed their practices to embrace PPMs, according to Steve Messinger, of consulting firm MedTactics, Arlington, Va.

In the early 1990s, practices were looking for capital to invest in technology, equipment and ancillary revenue sources. Older physicians sought ways to cash in their personal equity to finance a comfortable retirement.

"Now that the PPMs have dried up," Messinger says, "I still have the same issues."

Redmond, the pediatric ophthalmologist, in 1997 led the sale of Medical Center Clinic to one of the nation's largest PPMs: Nashville, Tenn.-based PhyCor.

"We saw certain challenges in the marketplace, and one of the main ones was capital," Redmond says. "We thought PhyCor could bring it to us, and they thought they could, too. (But) the execution did not work out."

He says physicians grew increasingly unhappy as their incomes began to drop because,

as PhyCor employees, they had no incentives to trim expenses and grow profits. So practitioners began to buy their way out of their 40-year management contracts.

"Everyone was getting out for the same reason, just like everybody got in for the same reason," Redmond says. "It became sort of a stampede at the end of 2000."

Redmond says the need for realistic expectations about business performance became apparent once the government began cutting Medicare reimbursement rates after 1997.

Subsequently, the Stark laws governing self-referrals, declining commercial reimbursements, soaring medical malpractice costs and HIPAA have prompted the doctors to refocus on the fundamentals of what made them successful in the first place.

"It's just back to basic blocking and tackling," Redmond says.

Under PhyCor, accounts receivable took more than 80 days on average to collect. Redmond says that number has since dropped to the mid-50s.


HAIDER

"We're doing much better now," he reports. "We changed our compensation plan. We have cost-accounted everything back to the individual department and to the physicians. The physicians are highly incentivized to watch their expenses very carefully."

BACK TO THEIR ROOTS

Redmond's experience at Medical Center Clinic is typical, says Messinger, in that the physicians aimed to recapture the culture of their group when they took back financial control from the PPM.

"Better-performing groups have a strong sense of culture and mission, great retention of physicians, great leadership and strong management," Messinger says. "Performance trends parallel leadership, governance and cultural issues much more than size or specialty."

That notion got lost sometime in the mid-1990s, when the PPMs were snapping up practices with the promise that physicians could forget about paperwork and concentrate on delivering care.

"Of course, that was an attractive-sounding argument at the time," says Kamal Haider, M.D., board president of the 50-year-old Clark and Daughtrey Medical Group, a former affiliate of failed multispecialty PPM, MedPartners.

Clark and Daughtrey grew from about 20 physicians when it joined the PPM in late 1995, to 40 a year and a half later. Haider calls it "expansion without much thought."

The practice started negotiating an exit in 1998. The formal separation occurred in 1999, not long before MedPartners went bankrupt.

"Eventually, the realization for us was that the management had to be on-site—local and not distant," Haider says. "It's best for physician groups like us to retain control of the business part of the practice."

So after buying back their assets, practices reworked compensation plans to emphasize physician ownership and control.

One method that has worked, Messinger says, is for each physician to receive a budget for nurses, staff, equipment and other costs of practicing medicine. Anything left goes toward the doctor's salary, placing a premium on controlling expenses.

Business models based on service rather than ownership began to emerge in 1998—about the time a proposed $8.1 billion merger between PhyCor and MedPartners unraveled, symbolizing the turning point in the fortunes of the large PPMs.

"We had to go through the whole blowup before we could see new models," says Tim Schier, Houston-based vice president of New York healthcare investment banking and consulting firm Cain Brothers. ■

KPC itself filed for bankruptcy in November 2000 and sold the practices back to the physicians.

Even the specialty PPMs have undergone reinvention. Physicians helped executives of Physicians Resource Group, a failed ophthalmology PPM that did not employ physicians, buy out the information technology department and transform it into MediNetwork, a practice consulting firm in Dallas.

At one point, PRG had 160 practices, 300 locations, more than 600 physicians and 5,500 employees. "We ran all the internal systems and ran the practice management software for 40 practices," says Mark Johnson, former chief information officer of PRG and now president of MediNetwork, which today has a mere 21 employees.

Specialty Care Network SCN, a Lakewood, Colo., PPM that once owned the assets of 24 musculoskeletal practices comprising 183 physicians, tried to cash in on the dot-com boom in late 1999 by creating healthgrades.com, a consumer Web site that compiles quality data on physicians, hospitals and health systems.

Ironically, only the Web venture survives.

—N.V.

Metamorphosis of the PPMs

FROM		TO
MedPartners multispecialty	➤	**Caremark Rx** pharmacy benefits manager
	➤	**Team Health** hospital-based PPM
	➤	**KPC Medical Management** multispecialty PPM (bankrupt)
PhyCor multispecialty	➤	**Aveta Health** healthcare risk manager
Coastal Physician Group multispecialty	➤	**PhyAmerica Physician Group** emergency medicine PPM
Physicians Resource Group ophthalmology/optometry	➤	**MediNetwork** consulting firm
Specialty Care Network musculoskeletal medicine	➤	**healthgrades.com** consumer Web site
Raven Healthcare Management multispecialty	➤	**STAT Solutions** management service provider

Source: *Modern Physician* reporting