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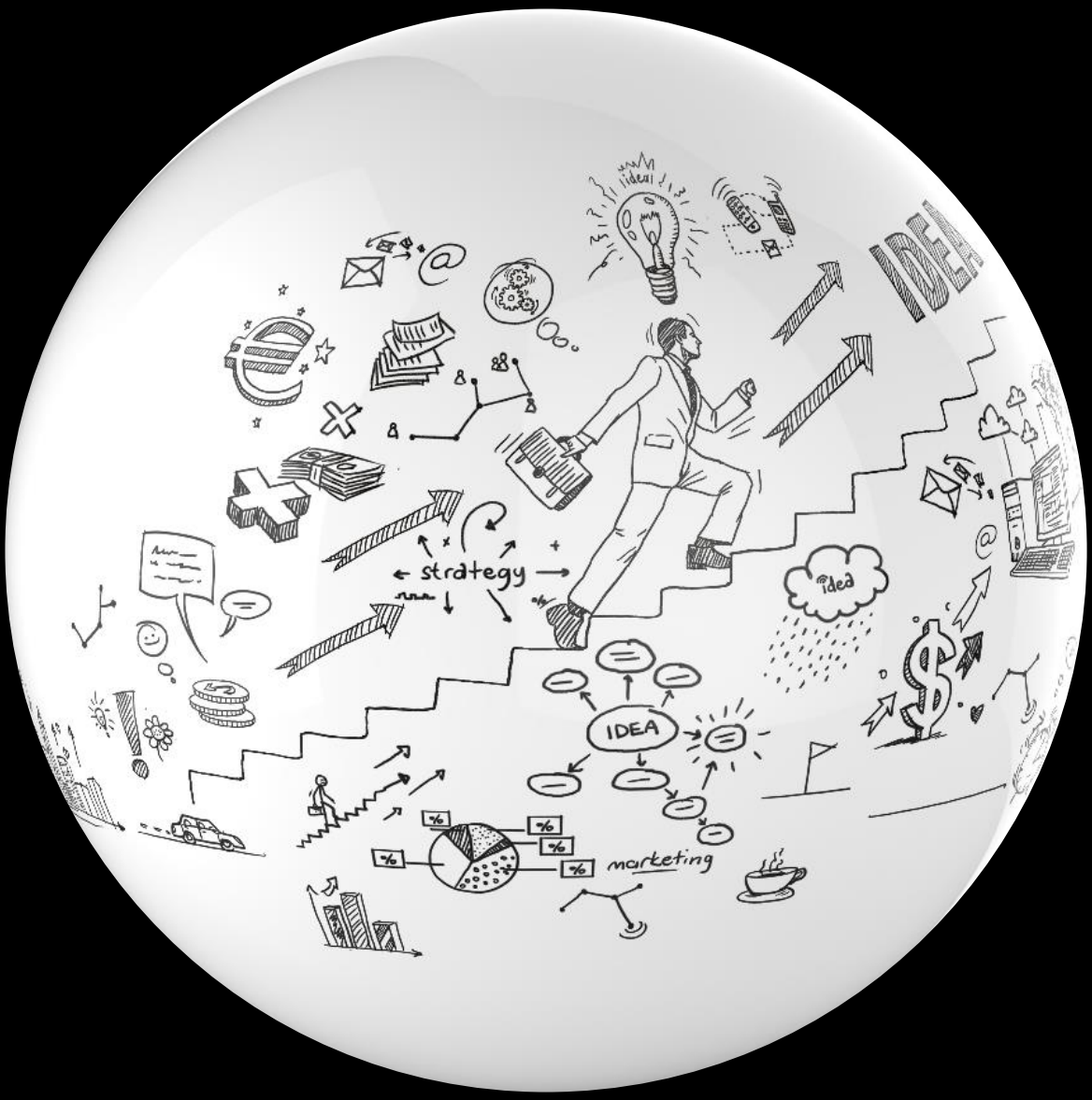

Diversifying Revenue for Health Systems Facing Fee-for-Service Headwinds

February 2024

Introduction

The US health care ecosystem is undergoing a wave of reassembly. Business models are changing, data is becoming more interconnected, and new disruptive players are emerging with a greater focus being placed on the empowered consumer. We see these forces of change being brought to bear through the proliferation of both *intra-industry* (e.g., health plans pursuing care delivery) and *inter-industry* convergence (e.g., outside companies like Apple or Amazon entering the health care space). Legacy health systems—who have long benefited from their established brands, strong market presence, and strong balance sheets—are feeling the pressure as new entrants from tech, retail, and private equity double down on their drive into the industry.

To respond to these changes, health system executives may be tempted to call upon strategies from their old playbooks: *Grow footprint through M&A; look for cost savings opportunities across the business;* or *negotiate better rates with payors*. Their challenge, however, is that the competitive landscape continues to evolve and demands a reexamination and refresh of those playbooks. By 2030, we expect much of the dust from industry reassembly to begin to settle, with several *new* incumbents emerging as the go-to names the average consumer thinks of for health care products and services. For those health systems who are widely considered today's incumbents, this wave of reassembly means it is time to start thinking differently about revenue streams ***now***.

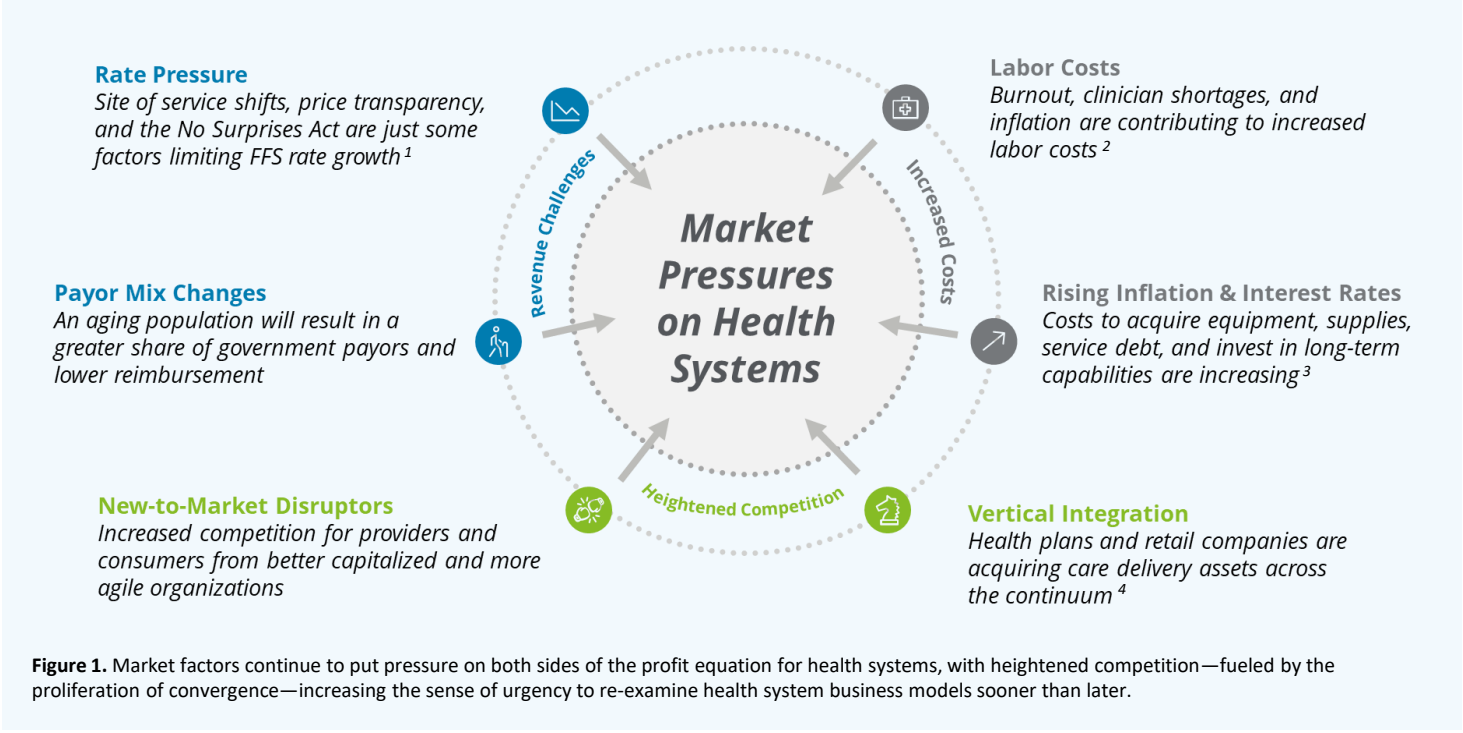

Figure 1. Market factors continue to put pressure on both sides of the profit equation for health systems, with heightened competition—fueled by the proliferation of convergence—increasing the sense of urgency to re-examine health system business models sooner than later.

Earlier this year we touched on the resurgence of provider-sponsored plans as a strategic path we're seeing provider systems take to diversify their revenue streams. Becoming a health plan enables provider systems to capture the full administrative and medical premium dollar but has proven to be challenging for many systems to be successful. It requires the right strategy, mature capabilities, different business and financial skills, and the right environment to be successful. While the health plan business will still be a worthy consideration for a subset of providers within the next few years, it is certainly not a silver bullet, nor is it for everyone. Here we discuss several other, near-term actions providers should take—including value-based contracting (VBC), consumer cash-based payments, and direct-to-employer contracting—to begin diversifying their traditionally fee-for-service (FFS) business, realize more immediate margin improvement, and prepare for higher levels of risk (*and reward*) down the road.

No Regrets Options for Diversifying Revenue

Integrated FFS & VBC Payor Contracting Strategy

As reimbursement models continue to expand beyond traditional FFS payment models toward value-based payments, many providers have already begun to diversify their revenue streams by participating in both FFS and VBC arrangements. Trying to balance the often-competing priorities of these arrangements has left providers struggling to fully maximize the revenues from these contradictory payment streams. This has created the need for providers to be **intentional in developing a more sophisticated, portfolio-based payor contracting strategy** that will allow them to optimize revenue capture and organizational margin through a combination of both payment models.

Providers can identify the right mix of FFS and value-based payments by leveraging an integrated financial model which enables optimization across pricing, value-based care structures, and operational performance.

An integrated financial model combines the power of analytics to evaluate a breadth of inputs, including the provider's competitive rate positioning and contract terms while factoring in the cost to serve their existing population, to assess their strategic levers, such as VBC strategy and prioritized payor partnerships. This allows a health system to project future revenue and profitability to identify a contracting strategy that optimizes future margins. This optimized contracting strategy should include both hospital-based and ambulatory services and account for potential shifts in volume between these settings as industry trends continue to favor lower cost of care settings.

Consumer Cash-Based Payments

While fee-for-service and value-based reimbursement models continue to be the dominant vehicles for how providers receive payments, a new generation of health consumers has emerged who seek to control their out-of-pocket spending through enrollment in high-deductible health plans. Add in a steady increase in the under-insured population and it has driven a growth in cash-based payments. Cash-based payments are occurring in a variety of settings, including primary, virtual, and urgent care centers, free-standing laboratory and imaging centers, and niche health startups, offering flexibility in how frequently services are utilized and reaching consumers who might otherwise be deterred by typical pricing models.

Providers can capitalize on this trend and further diversify their revenue streams by designing differentiated pricing for direct cash payments and increasing their service offerings at urgent care and free-standing imaging and procedure sites that tend to favor cash-based reimbursements. In addition to service offerings, **critical for success in a cash-based payment model are consumer-centric capabilities and services** (e.g., convenience, ease of access, personalization of patient experience) that rival those of retailers.

Direct-to-Employer Contracting

Providers can further differentiate revenue streams and the ways they interact with consumers across their health journeys through direct-to-employer contracting and employer-based services. Recent survey data points to growing interest among large, self-insured employers to contract directly with health systems for services, such as primary care—according to a 2021 survey from the Business Group on Health, "9% of large employers have directly contracted primary care models in select markets; another 17% are considering it[5]." As the cost of providing health insurance to employees continues to climb–Kaiser Family Foundation reports that employers pay $8,435 a year for individual insurance plans and $23,968 a year for family coverage[6]—**providers should anticipate a growing demand for innovative, direct-contracted models from employers who want to contain their costs.**

By contracting directly with employers, providers can improve margins by retaining revenue in-house versus passing it through an external health plan and expand their footprint by gaining new patients in the employees. This can be done by offering a portfolio of services for targeted conditions, such as heart-related conditions and orthopedics, at a bundled rate. Providers can also establish onsite or near-site facilities to provide retail health like services directly on large employer campuses as it will give them access to the employee population that will highly utilize that clinic for office visits, thus providing an additional stream of revenue.

Increasing employer-based service offerings can also serve as a **precursor to health plan revenue** as many of the operations necessary to support direct-to-employer contracting can also support long-term vertical integration.

Long-Term Considerations for Sustaining Diversified Revenue

As providers assess options for revenue diversification, considerations around a balanced revenue portfolio, end-to-end cashflows, operational readiness, and long-term strategy should be evaluated. To determine the optimal proportion of each revenue stream for margin improvement and mission advancement, providers and health systems must gauge the organization's appetite for strategic risk and diversification. In most cases, traditional margin improvement strategies to capture attributed lives, achieve value-based targets, and create "stickiness" within the health system will remain necessary alongside more diversified sources of revenue.

For long-term financial sustainability providers should rethink not only how revenues are generated but also how cashflows are distributed throughout their system. The downstream flow of funds should support the updated revenue capture strategy—reinvesting in the capabilities needed to succeed across the identified combination of integrated FFS, VBC, cash-based, and direct-to-employer payment models, while restructuring physician contracts to incentivize improvements in both quality and total cost of care.

It is also critical that providers ensure their operational readiness for each new revenue stream. Lagging capabilities must be addressed to position health systems for long-term financial viability while also generating return in the short term. This kind of care model transformation often includes optimizing current data and reporting capabilities, creating a cohesive provider network strategy, and streamlining workflows across core functions, such as care management, quality improvement and performance management, and administration (i.e., supply chain and marketing).

Closing

As the center of gravity for US health spend continues to shift away from sick care and toward health and well-being, traditional providers that depend on acute and episodic conditions will continue to see their revenue opportunities erode over time. The winners will be those organizations that act now to prepare for the revenue shifts to come, in terms of ***how*** payments are exchanged and ***where***, as well as determine ***who*** is making spending decisions in the future. Doing so requires a diversification of today's services *and* revenue streams - likely through a combination of the strategic paths described above.

Innovative partnerships will be as important as ever for health systems to pursue these strategies for revenue diversification, and to orient their services around the consumer. Consistent and easy consumer engagement will win the day, and disruptive thinking, as well as a diversified portfolio, will be critical for provider organizations to continue to remain competitive in today's evolving and reassembling landscape of health.

Reach out for a conversation

To learn more about how your organization can leverage population health strategies to diversify revenue streams, please contact:

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If you are interested in learning more, we invite you to read the other Deloitte articles referenced in this piece:

Advancing value-based care within health care strategy

https://www2.deloitte.com/us/en/pages/life-sciences-and-health-care/articles/provider-sponsored-health-plans.html

Optimizing care model transformation and redesign

https://www2.deloitte.com/us/en/pages/life-sciences-and-health-care/articles/care-model-transformation.html

End Notes

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