ECONOMIC ANALYSIS OF THE TENTATIVE PHYSICIAN SERVICES AGREEMENT

by

Jack L. Carr*

August 8, 2016

*** Professor Emeritus of Economics, University of Toronto**

BACKGROUND

I am a Professor Emeritus of Economics at the University of Toronto (150 St. George Street, Toronto, Canada, M5S 3G7), where I have taught since 1968. I am also a former acting Chair of the Department of Economics and a former Director of Graduate Studies. I have a B. Com. degree from the University of Toronto and an M.A. (Economics) and Ph.D. (Economics) from the University of Chicago. My research and teaching interests focus primarily on monetary economics, financial economics and law and economics. I attach a copy of my curriculum vitae which summarizes my research and teaching experience.

EXECUTIVE SUMMARY

1. Vagueness of the TPSA

Unlike previous PSAs, the TPSA has very little detail in it. It is not clear how this co-managed system will operate and a large amount of the actual implementation of the TPSA will be determined sometime in the future.

2. Ignoring Effects of Inflation

This agreement provides for an increase in funding for the Physicians Services Budget (PSB) of 2.5% in each of the four Fiscal Years of this agreement. This increase in funding is in what economists call nominal dollars and does not in any way consider the effects of inflation. It is reasonable to expect inflation in Canada to be about 1.5% to 2%. At an inflation rate of 2%, an increase in the PSB of 2.5% is only a real increase of 0.5% per year. It is difficult to see how real increases in funding of 0.5% can pay for the health care needs of a growing and ageing population and for the cost of new physicians. If the real increases of 0.5% prove inadequate, then the TPSA mandates for further cuts in funding (in addition to the $200 million dollar cuts in funding already provided in the agreement).

3. Doctors Assume Financial Responsibility for Increased Usage in System

The TPSA is an historic agreement in that it makes doctors financially responsible for increased usage in the system due to a growth in population and due to an ageing in the population and due to net increases in the number of physicians. By agreeing to the TPSA the doctors implicitly accept financial responsibility for increased utilization. Any increase in utilization over and above that provided for in the PSA, is the financial responsibility of the doctors.

4. Does Not Provide For System Stability

If utilization rates increase above 3.1%, there will be substantial and significant payment reductions. This report shows that for an increase in utilization rates of 4% per year, there is a total payment reduction in the four years of $981.1million and if there is an increase in utilization rates of 5%, there is a total payment reduction of $2.1244 billion. The TPSA does <u>not</u> guarantee a period of stability.

5. Negatively Affects Patient Accessibility

From an economic point of view, if payments to doctors decrease this ultimately will affect physician supply and availability of medical services to the residents of Ontario. **Cuts in physician payments will clearly negatively impact patient accessibility.**

INTRODUCTION

I have been requested by the Coalition of Ontario Doctors to do an economic analysis of the 2016 Tentative Physician Services Agreement (TPSA).

ECONOMIC ANALYSIS OF TPSA

The following are my comments on the TPSA.

1. Vagueness of the TPSA

Unlike previous PSAs, the TPSA has very little detail in it. The TPSA states that "....[t]he Parties agree that they have a joint responsibility to hold expenditures for physician services to the planned PSBs in each Fiscal Year and the Parties will use the co-management process to achieve the goals of this PSA." In the first place, it is not clear how this co-managed system will operate. In the second place, a large amount of the actual implementation of the TPSA will be determined sometime in the future. The co-managed process will determine the extent of any future cuts and exactly how any future cuts will be implemented. The lack of the specificity in this agreement makes it difficult to do a complete economic analysis of this agreement.

2. Ignoring Effects of Inflation

This agreement provides for an increase in funding for the Physicians Services Budget (PSB) of 2.5% in each of the four Fiscal Years of this agreement ".....to pay for the health care needs of a growing and ageing population and the MOHLTC's share of the cost of net new physicians." This increase in funding is in what economists call nominal dollars and does not in any way consider the effects of inflation. Currently inflation, as measured by changes in the Consumer

Price Index (CPI), is running at 1.5% per year (ie. the increase in the CPI from June 2015 to June 2016 is 1.5%). The Bank of Canada is currently committed to keeping inflation in Canada at between 1% and 3% and the middle of that range is 2.0%. As such, it is reasonable to expect inflation in Canada to be about 1.5% to 2%. At an inflation rate of 1.5%, an increase in the PSB of 2.5% is only a <u>real</u> increase of 1% per year (ie. funding is <u>only</u> allowed to increase at a rate of 1% per year over and above inflation). At an inflation rate of 2%, an increase in the PSB of 2.5% is only a real increase of 0.5% per year.

It should be noted that from 2001 to 2014 Physicians' Overhead Costs have increased by about 1.7% <u>over and above</u> the inflation rate. This increase in real overhead costs will also result in a <u>real</u> decrease in the net compensation of physicians.

It is difficult to see how real increases in funding of between 0.5% and 1% can pay for the health care needs of a growing and ageing population and for the cost of new physicians. Every year 140,000 new patients come into the health care system in Ontario. Every year there is a net increase of about 700-800 new physicians.

If the real increases of 0.5% to 1% prove inadequate, then the TPSA mandates for further cuts in funding (in addition to the $200 million dollar cuts in funding already provided in the agreement).

3. Doctors Assume Financial Responsibility for Increased Usage in System

The TPSA is an historic agreement in that it makes doctors financially responsible for increased usage in the system due to a growth in population and due to an ageing in the population and due to net increases in the number of physicians. By agreeing to the TPSA the doctors implicitly accept financial responsibility for increased utilization. Any increase in utilization over and above that provided for in the PSA, is the financial responsibility of the doctors. If for example, the government decides to bring in more refugees to Ontario who have significant medical care needs, the terms of the TPSA make the doctors financially responsible for this increased usage rather than this being a government responsibility. If the Ontario economy grows and attracts new residents from other provinces, once again the doctors bear financial responsibility for increased growth over and above what is planned for in the TPSA.

The TPSA is unlike any other labour agreements in the provinces. Would the teachers in this province ever sign an agreement with the government which states that if the growth in student population is above expectations, teachers would be required to take across the board pay cuts to finance the unexpected increased enrollment? Would the government ever ask the teachers to sign such an agreement? The TPSA is a unique labour agreement.

The expectation that overall the TPSA provides for adequate funding and will not require any further cuts (other than the $200 million cuts provided for in the TPSA) depends on the assumption that utilization rates will increase by 3.1%. If utilization rates increased by more than 3.1% then further cuts in doctor funding will be required. It should be noted that for 2016/17 the TPSA does not allow for any cuts in excess of the one-time payment of $50 million. This cap on funding reductions does not apply in the other years. There is no restriction on cuts in the other three years.

In 2014-2015, utilization rates increased by 4.6%. I consider two scenarios for increases in utilization rates.

(i) Scenario A

In Scenario A, I consider an increase in the utilization rate of 4% per year. In this scenario, the table below shows that in 2019/20, there is a necessary fee cut of $448.6 million. It is unknown at the current time how such a fee cut would be implemented, but if this cut was an across the board fee cut, a cut of $448.6 million represents a reduction of 3.5% in total doctor compensation. In the four years from 2016 to 2020, there is a need for total fee cuts of $981.1 million in addition to the $200 million in cuts already in the TPSA. It should also be noted that this calculation of total fee cuts <u>does not</u> include any of the fee cuts that were made prior to this agreement. These previous fee cuts are now a permanent feature of the system.

SCENARIO A: ASSUMING 4% ANNUAL INCREASE IN UTILIZATION
MILLIONS OF DOLLARS

FISCAL YEAR	**FUNDED GROWTH INCLUDING ONE TIME**	**FORECAST PSB**	**ONE TIME ACTUAL**
2016/17	$11,936.6	$12,047.4	$ - 50.0*
2017/18	12,270.4	12,425.3	-154.9
2018/19	12,594.7	12,922.3	-327.6
2019/20	12,886.6	13,335.2	-448.6
TOTAL			**$-981.1**

* Maximum allowed for 2016/17.

(ii) Scenario B

In Scenario B, I consider an increase in the utilization rate of 5% per year. In this scenario, the table below shows that in 2019/20, there is a necessary one-time fee cut of $973.4 million. It is unknown at the current time how such a one-time fee cut would be implemented, but if this cut was an across the board fee cut, a cut of $973.4 million represents a reduction of about 7.6% in total doctor compensation. In the four years from 2016 to 2020, there is a need for total fee cuts of $2.1244 billion in addition to the $200 million in cuts already in the TPSA. Once again, it should also be noted that this calculation of total fee cuts does not include any of the fee cuts that were made prior to this agreement. These previous fee cuts are now a permanent feature of the system.

SCENARIO B: ASSUMING 5% ANNUAL INCREASE IN UTILIZATION
MILLIONS OF DOLLARS

FISCAL YEAR	**FUNDED GROWTH INCLUDING ONE TIME**	**FORECAST PSB**	**ONE TIME ACTUAL**
2016/17	$11,936.6	$12,163,2	$ - 50.0*
2017/18	12,270.4	12,666.4	-396.0
2018/19	12,594.7	13,299.7	-705.0
2019/20	12,886.6	13,860.0	-973.4
TOTAL			**$-2,124.4**

* Maximum allowed for 2016/17.

4. Does Not Provide For System Stability

The OMA has stated that "...the tentative Physicians Services Agreement provides a much needed period of stability for the profession while the Charter Challenge continues through the court system". The TPSA restricts payment reduction to doctors to 50 million dollars in

2016/17. In the other three fiscal years there is no restrictions on payment reductions. If utilization rates increase above 3.1%, there will be substantial and significant payment reductions. This report already shows that for an increase in utilization rates of 4% per year, there is a total payment reduction of $981.1million and if there is an increase in utilization rates of 5%, there is a total payment reduction of $2.1244 billion.

The TPSA does not guarantee a period of stability.

5. Negatively Affects Patient Accessibility

From an economic point of view, if payments to doctors decrease this ultimately will affect physician supply and availability of medical services to the residents of Ontario. **Cuts in physician payments will clearly negatively impact patient accessibility.**