

Critical Strategies for Achieving Positive Medicare Margins

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Overview

- Hospitals face unprecedented pressures and uncertainty, and must understand the challenge they face
- Surviving requires getting the basics right as well as exploring emerging integrated models & partnerships
- Even today, there is significant potential locked up in traditional operating margin levers
- Ultimately, hospitals need to develop a balanced portfolio of initiatives to meet projected financial challenges

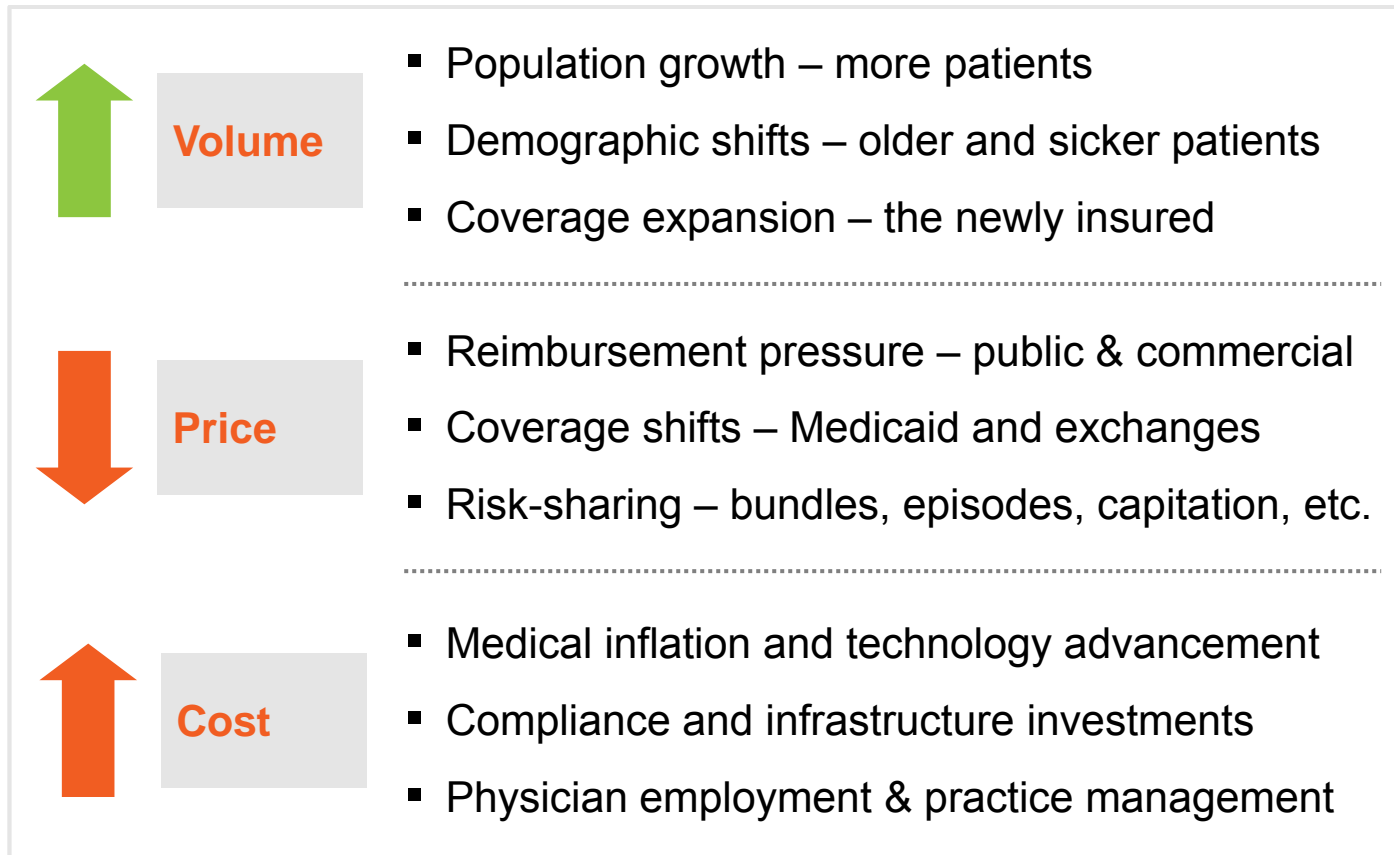


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Critical Strategies for Achieving Positive Medicare Margins

- **Pressures and uncertainty**
- Surviving and thriving
- Operating margin levers
- A balanced portfolio of initiatives

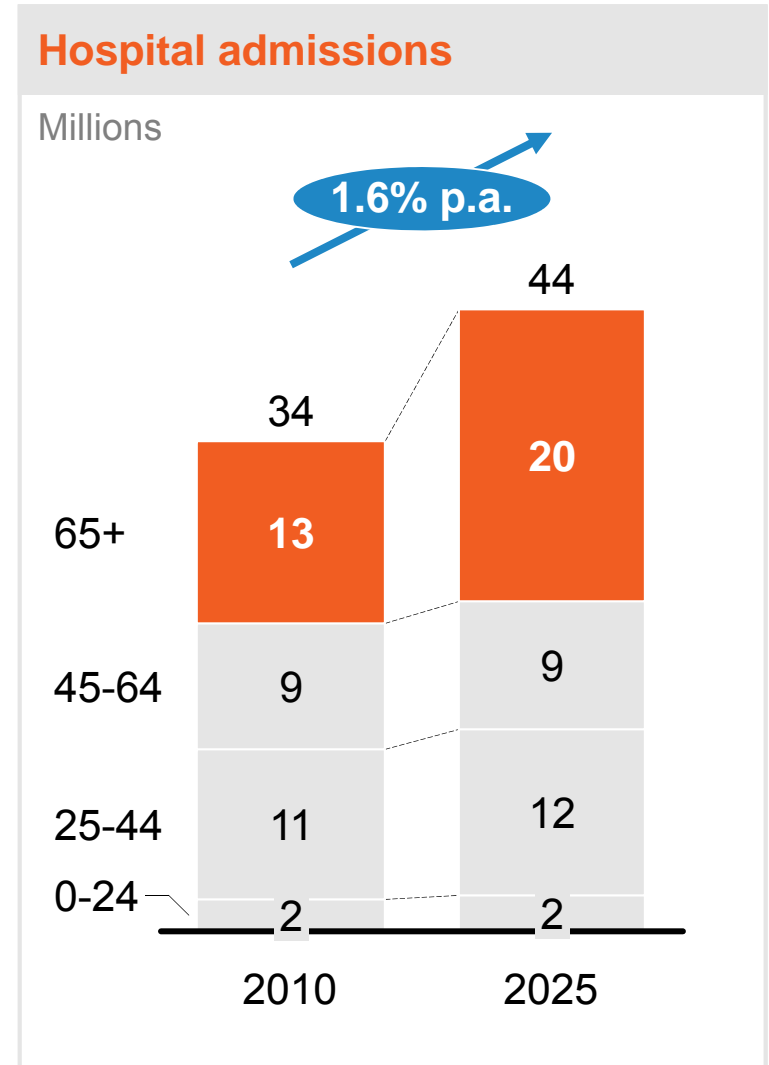
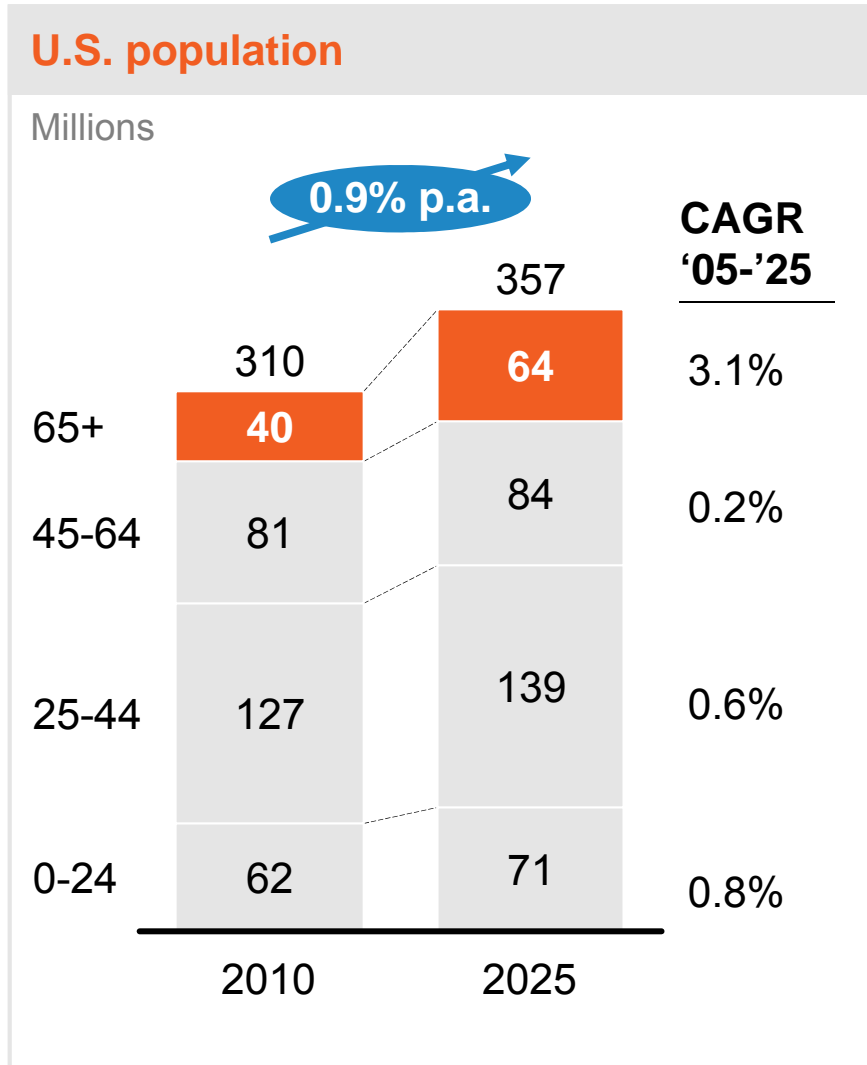
Hospitals face unprecedented pressures and uncertainty



Which one of the following is expected to have the biggest impact on revenue over the next 10 years at your hospital?

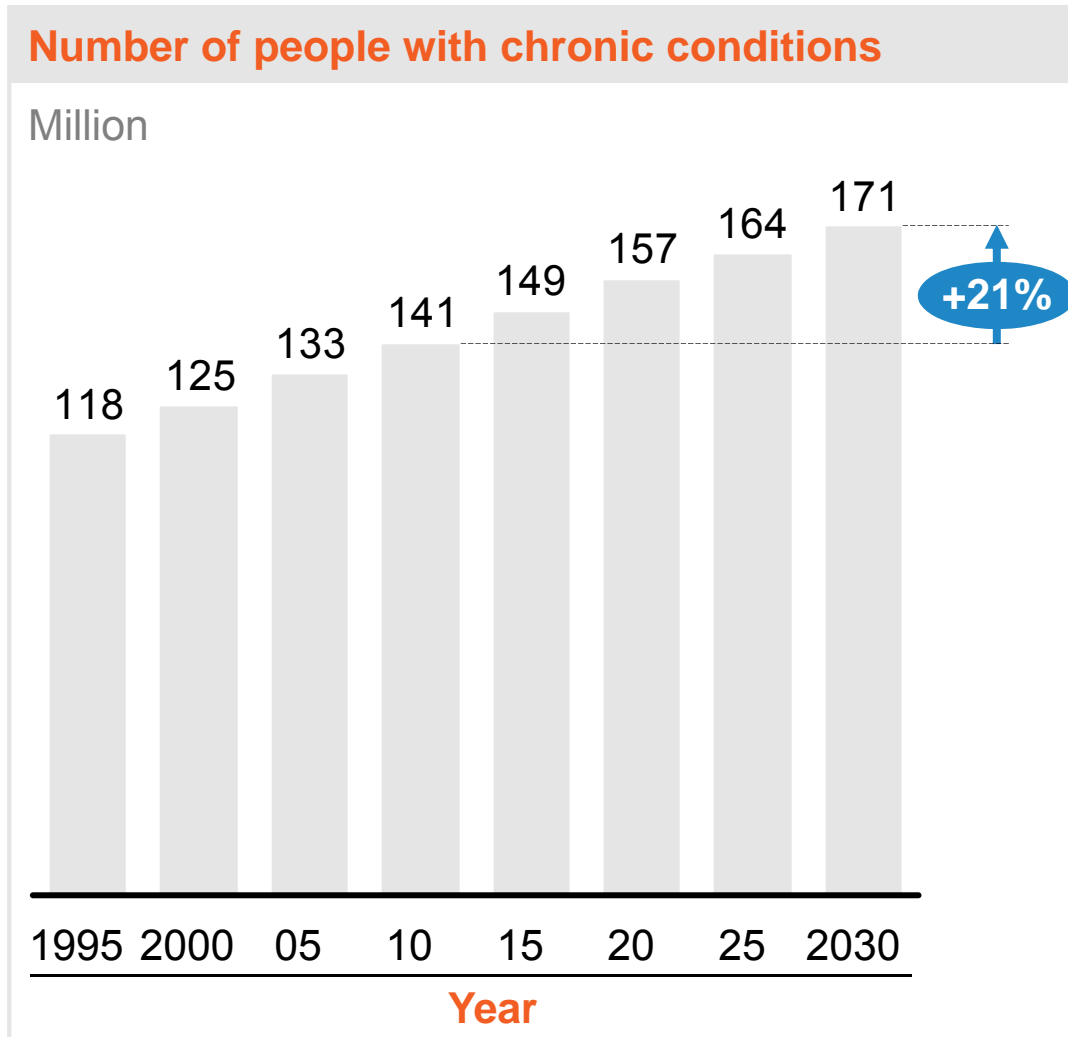
- A. Population growth
- B. Demographic shifts
- C. Coverage expansion
- D. Coverage shifts
- E. Reimbursement pressure

Volume will continue to climb, as population grows and Boomers age...



SOURCE: U.S. Census Bureau; NCHS 2007 National Hospital Discharge Survey

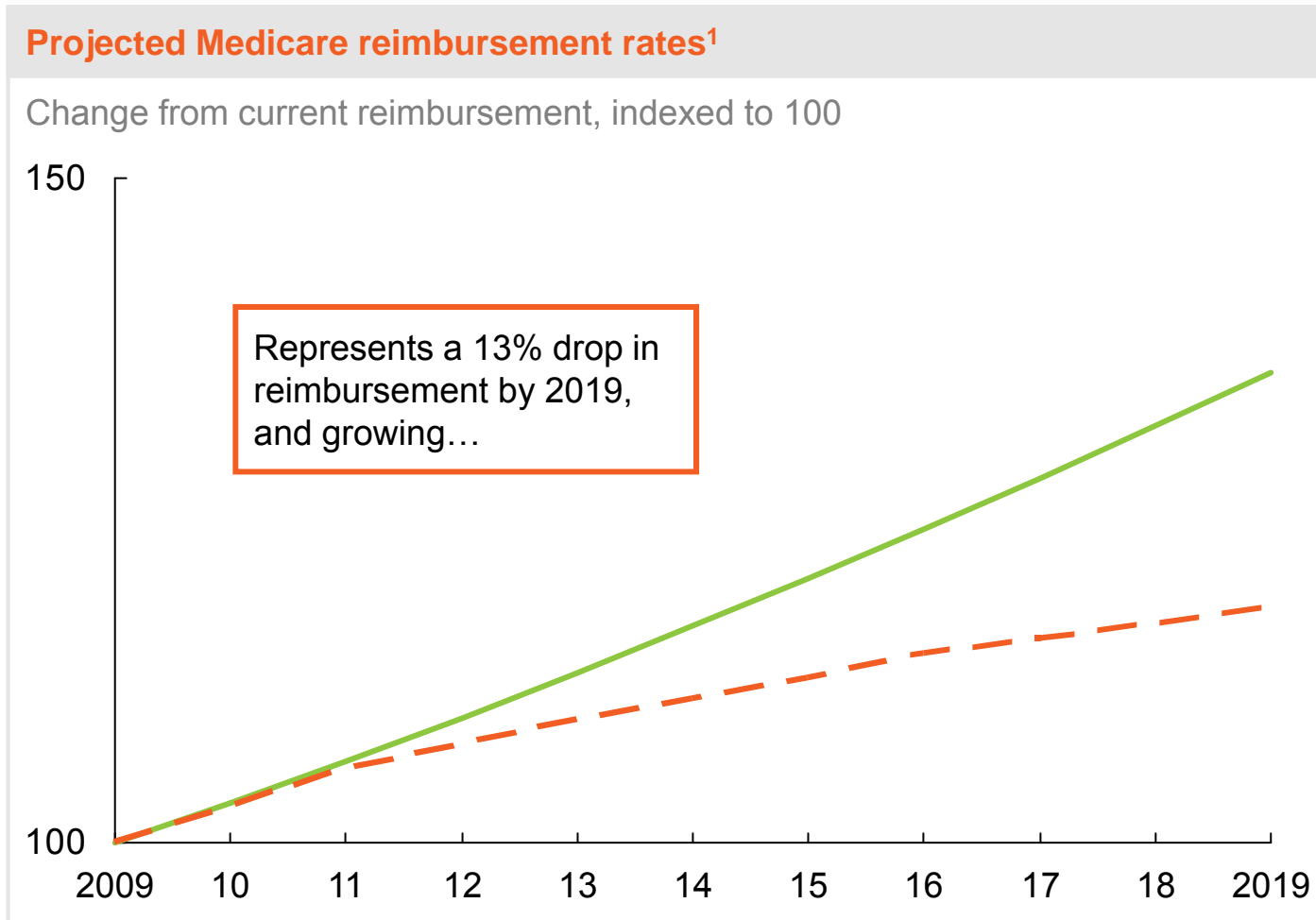
... and as the chronic disease burden continues to grow



- Between 2010 and 2030, the number of Americans with one or more chronic conditions will increase by **30 M**
- By 2020, **80 M** people will have two or more chronic conditions
- By 2020, projections indicate that the U.S. will spend nearly **\$700 B a year** in direct medical costs for persons with chronic diseases

Reimbursement pressures will increase over time, in part due Medicare reimbursement policies set in the Affordable Care Act

— No reform
- - Reform



¹ 2% reduction assumes the overall CMS budget reduction of 2% results in a 2% reduction in hospital payments



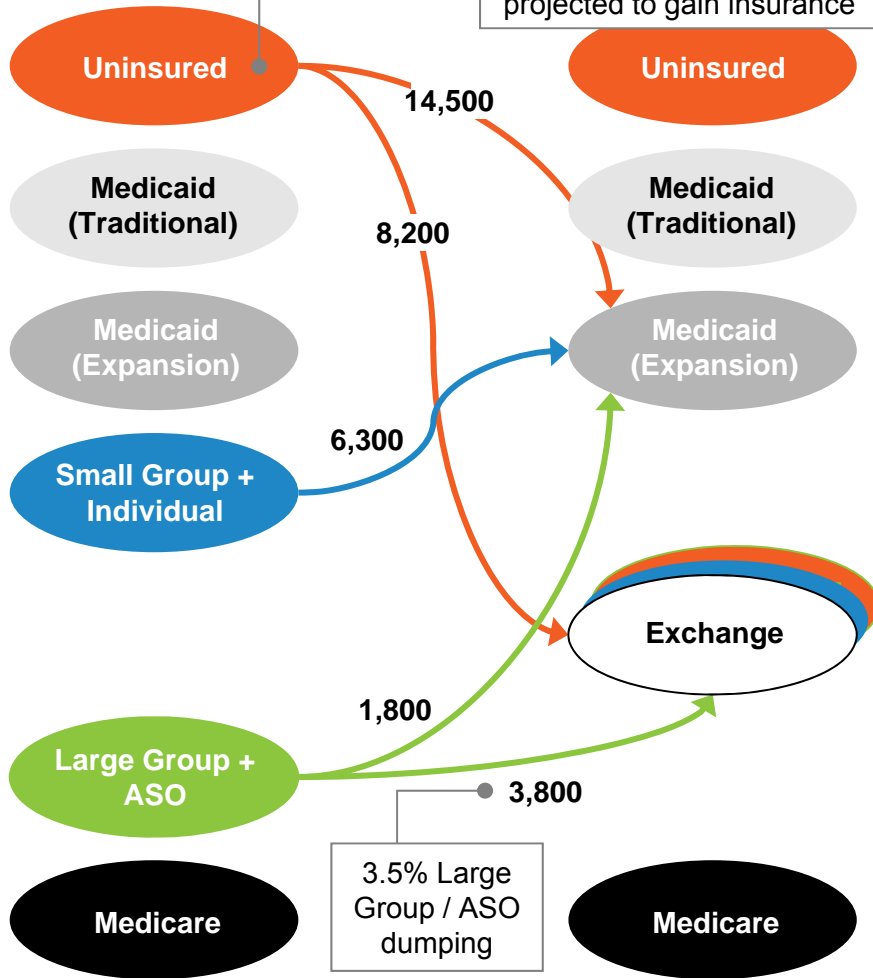
12 million commercial lives will shift to Medicaid and Exchange

MARKET EXAMPLE

Key coverage shifts

Lives; 2009-2016 (Reform)

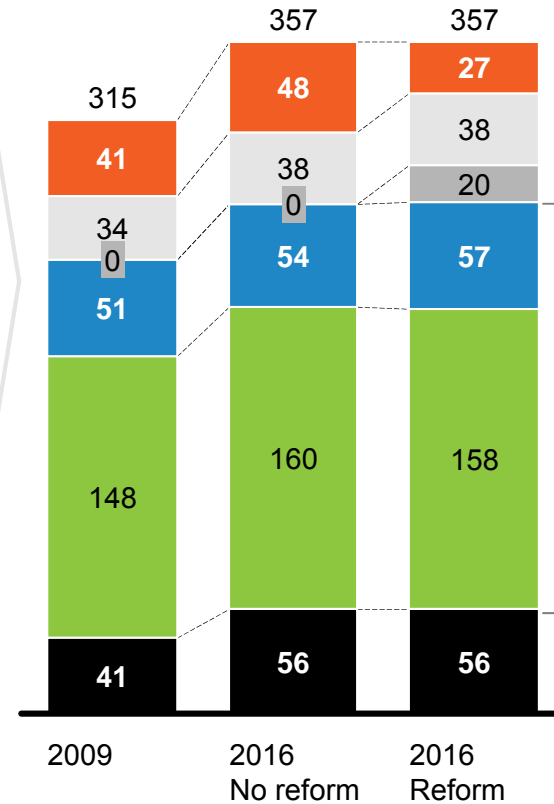
~45% of the uninsured are projected to gain insurance



Population by payor

Thousands of lives

- Uninsured
- Medicaid (Traditional)
- Medicaid (Expansion)
- Small Group / Individual
- Large Group / ASO
- Medicare

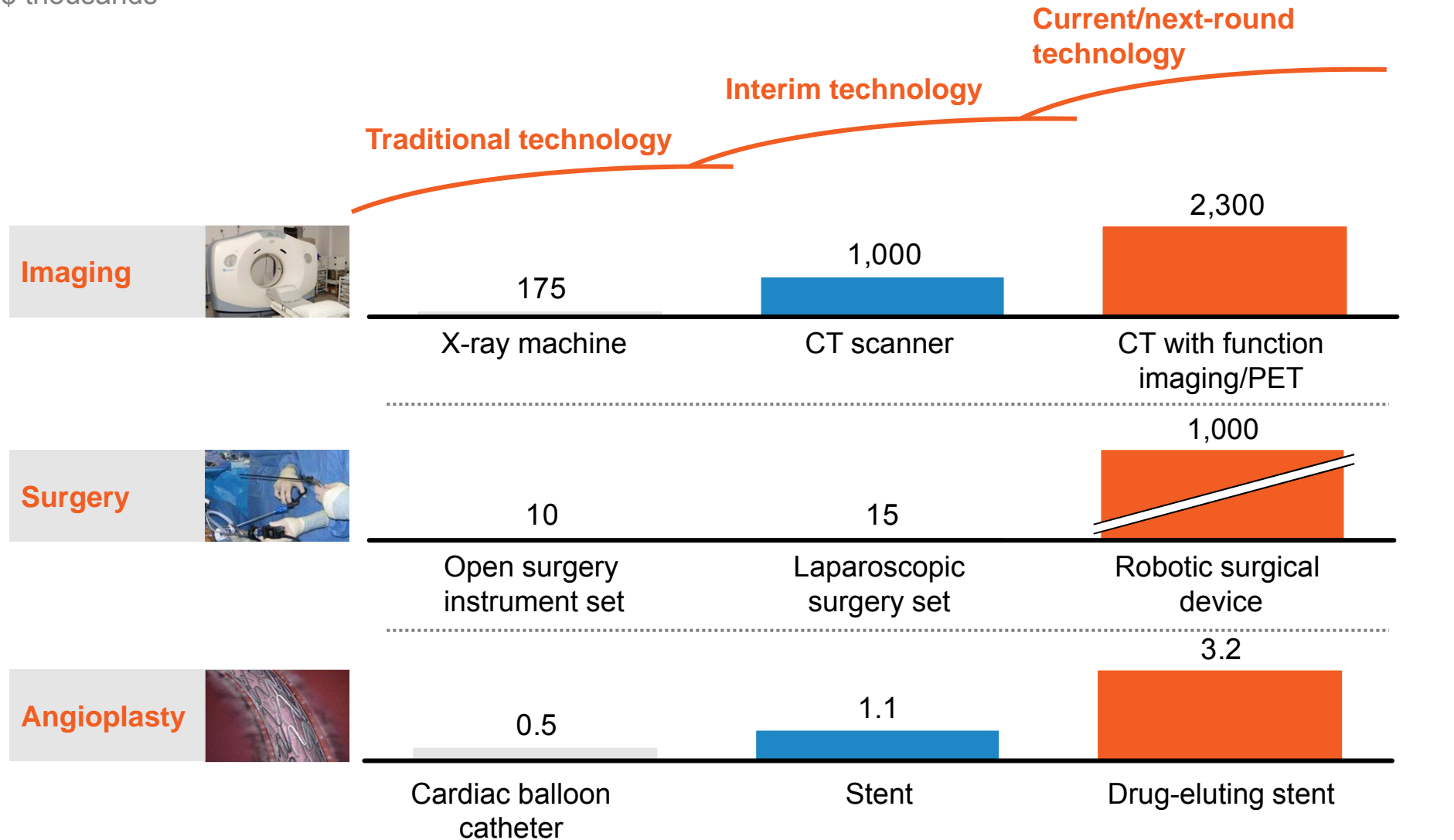


Small group and individual buy through Exchange post-reform

Total commercial: 215,000
(1.1% CAGR from 2009)

Cost trends continue to increase over time as we continue to adopt newer, more expensive technologies

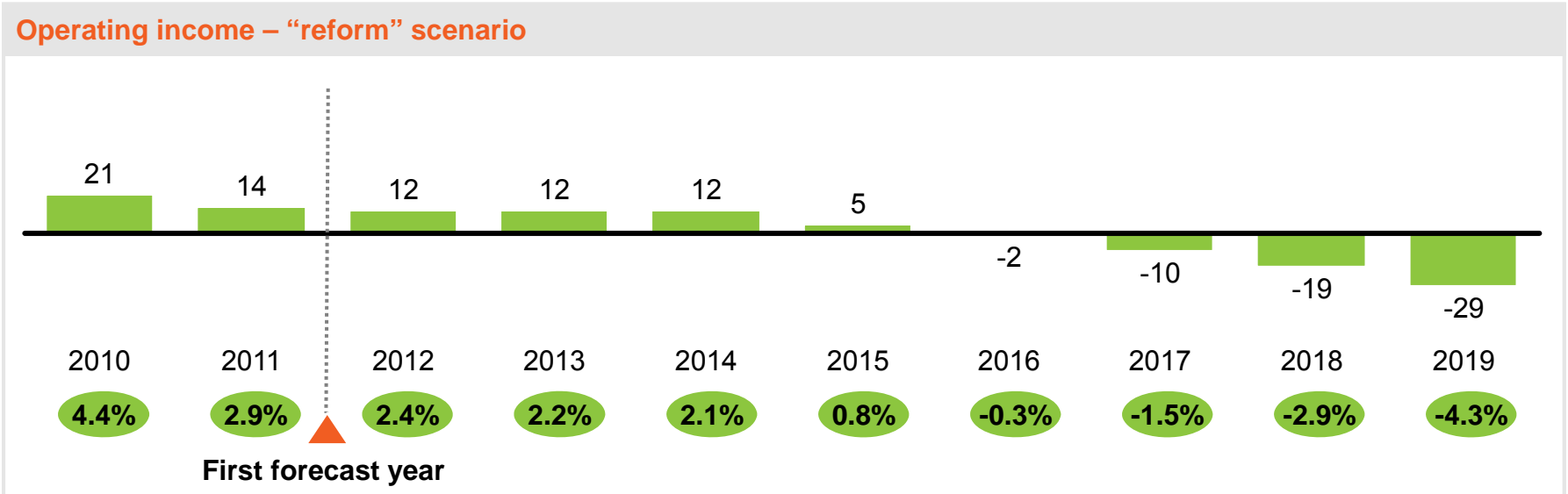
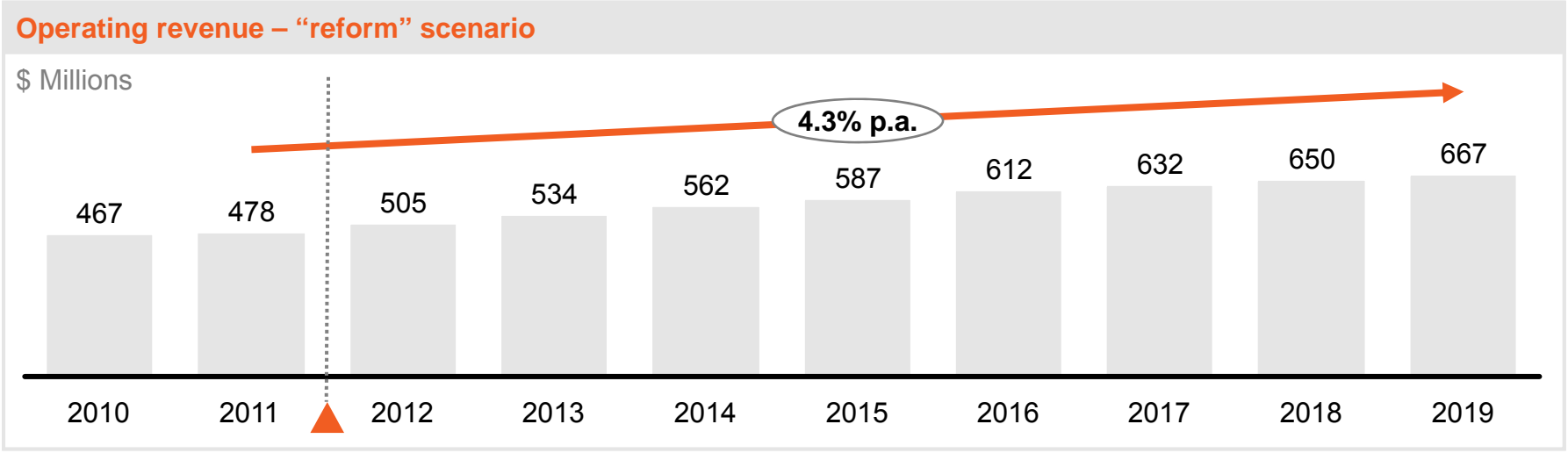
\$ thousands



Hospitals must understand and evaluate the impact of these trends, and the financial “gap” they will create

ILLUSTRATIVE

- Operating revenue
- Operating income
- Operating margin

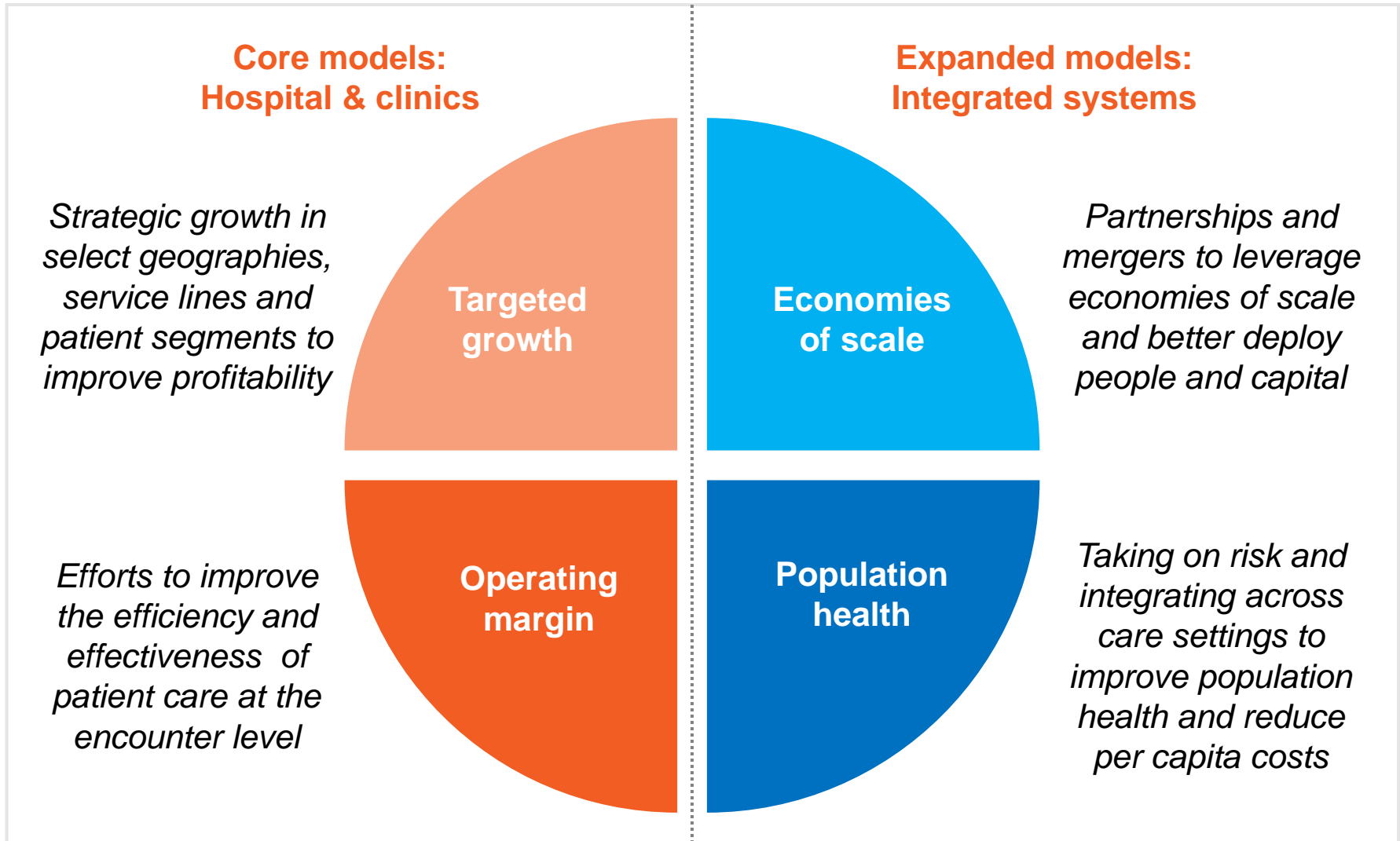


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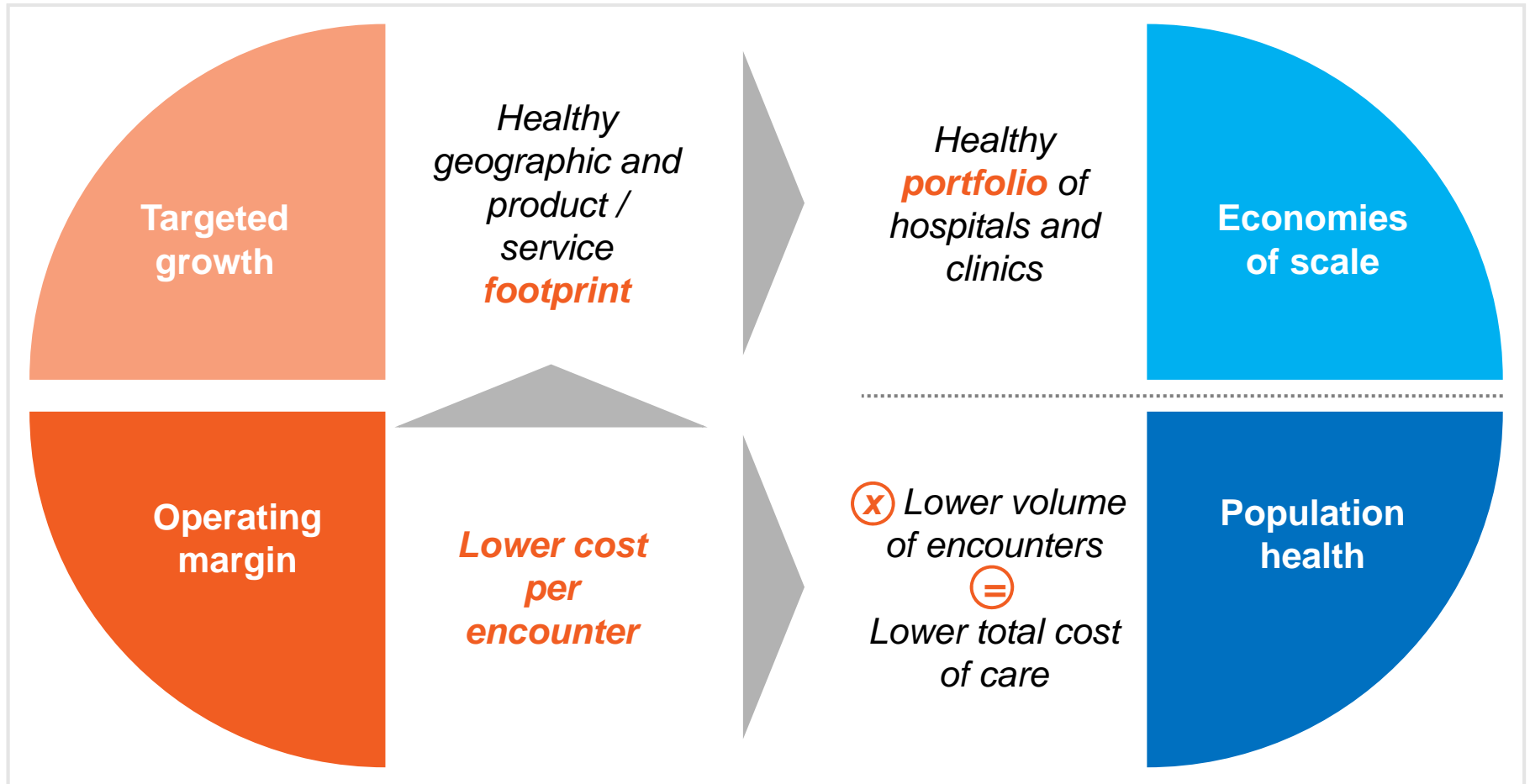
Critical Strategies for Achieving Positive Medicare Margins

- Pressures and uncertainty
- **Surviving and thriving**
- Operating margin levers
- A balanced portfolio of initiatives

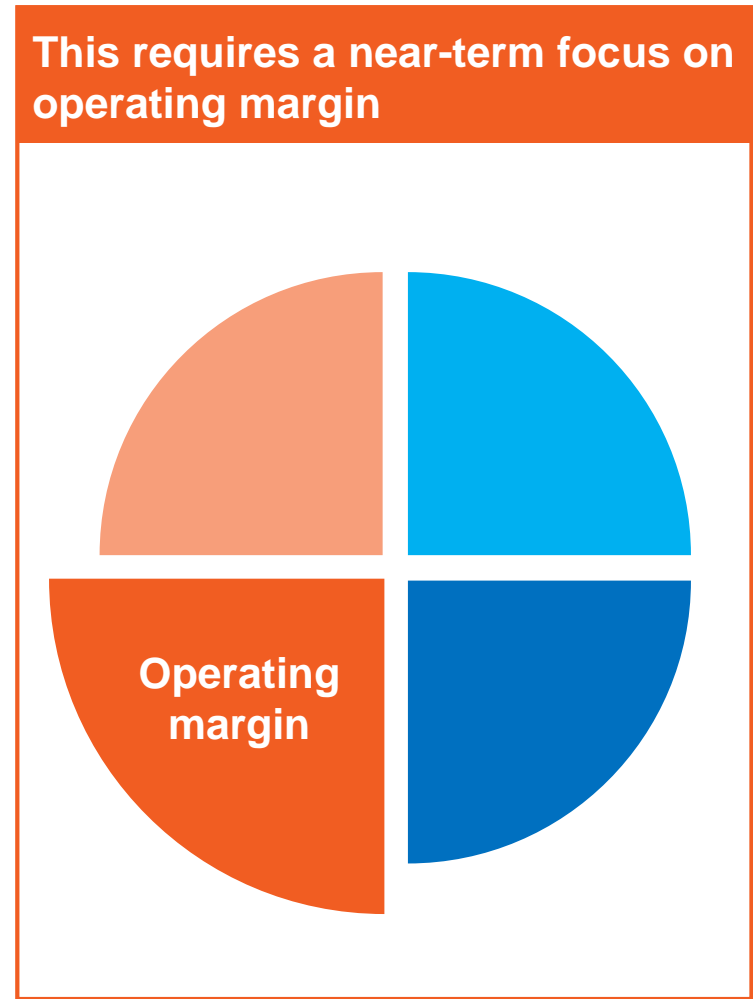
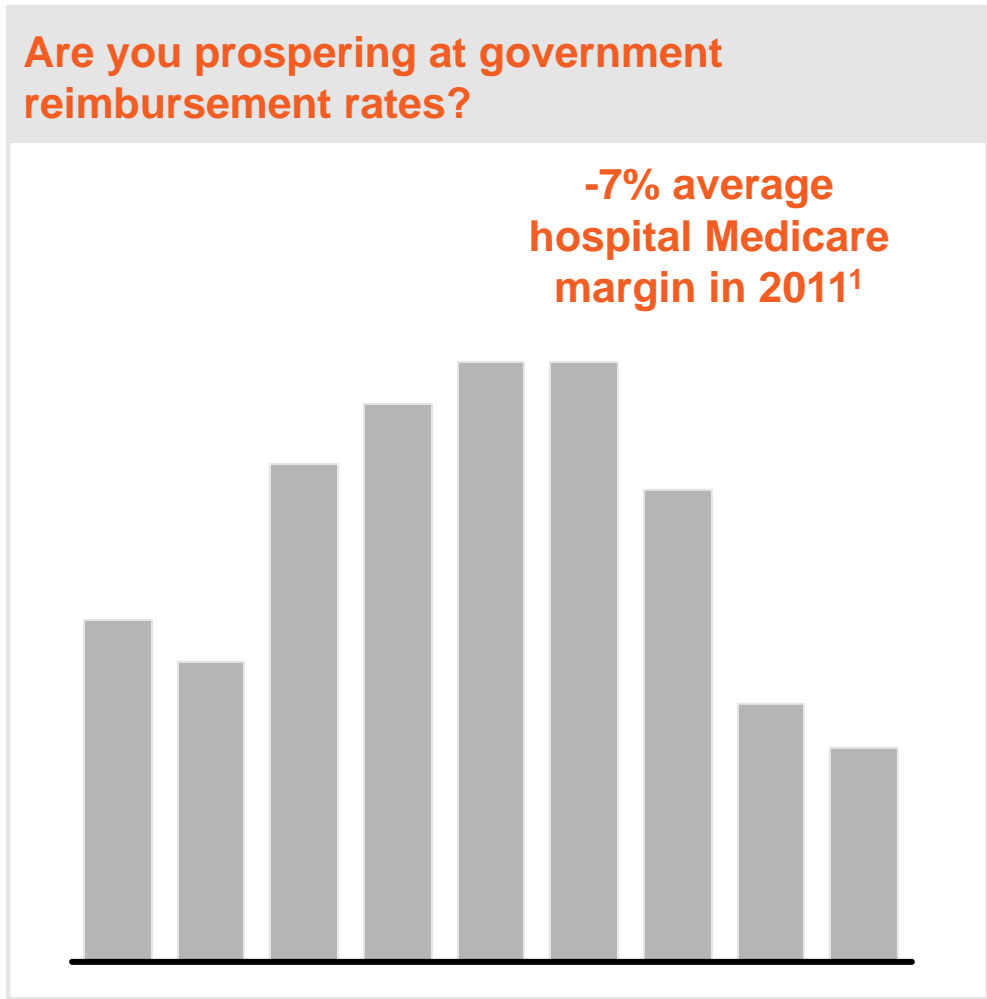
Surviving requires getting the core right as well as exploring expanded models



Expanded models will depend on hospitals getting the basics right



Consequently, positive Medicare margins has become an industry mantra



1 Medicare Payment Advisory Commission, Report to Congress: Medicare Payment Policy, March 2011



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Operating margin

Focus on five fundamental levers to improve margins

How well are you collecting on what you've earned?

Revenue cycle management

How efficiently and effectively are you running your facilities?

Clinical/admin operations

Labor productivity

Materials management

How engaged, efficient and effective are your physicians in delivering care?

Clinical variation



Revenue cycle management

1 **Increase payor yield**

2 **Reduce self pay impact**

3 **Improve cash collection**

4 **Charge optimization**

5 **Reduce costs**

- Has received Increasing attention over the last 5-10 years and
- Will become increasingly important as co-pays, deductibles, and BAI increase
- Once innovative processes are becoming increasingly standard
- Outsourcing / management services becoming more common & effective
- Opportunities can be very significant

Operations

Operating system

- 1 ■ The practices and procedures that drive patient throughput, focusing on the OR, ED, Floors, & Imaging

Management infrastructure

- 2 ■ The availability, tracking and sharing of data on a regular basis

Mindsets and behaviors

- 3 ■ The culture of leadership and staff, which are essential to achieving and sustaining high performance

- Established lever that has received lots of attention over last 2 decades
 - Virginia Mason Medical Center
- Most operational efforts fail
 - Identifying issues is easy
 - Prioritizing focus can be challenging
 - Implementing and sustaining is hard
- Significant pockets of opportunity remain at most healthcare institutions

Labor and productivity

1 FTE Volume & productivity

2 Wage rate & overtime use

3 Skill mix – admin and clinical

4 Turnover and development

- Labor is a hospital's largest cost center
- About much more than FTE's
- External benchmarks difficult to apply
 - Lots of benchmarks exist
 - Truly comparable data hard to get
 - Internal benchmarks emerging
- Hesitancy to address staffing issues
- Significant opportunities remain to address efficiency and effectiveness

Materials management

1 Formulary utilization

2 Vendor management

3 Pricing optimization

- A second major cost center
- Often high-performing function
 - Experienced teams
 - Established processes
 - Strong partners
- Pockets of opportunity typical, focused in one area or another
- Next frontier is closer management of clinical choices and decisions
 - Formulary management established
 - Drug substitutions emerging...
- Success is dependent on physicians

Clinical variation

1 **By department**

2 **By division**

3 **By diagnosis / procedure**

4 **By physician**

- Close management of clinical variation is the next frontier for many systems
 - Cost and quality
 - Population health
- Can be uncomfortable for both administrators and physicians
 - Mutual trust and engagement
 - Case for change
 - Clear objectives, targets & metrics
- Most only scratching the surface
 - Preference items
 - Standard practices and processes

Which of these areas presents the largest opportunity for margin improvement at your hospital?

- A. Revenue cycle
- B. Operations
- C. Labor productivity
- D. Materials management
- E. Clinical variation

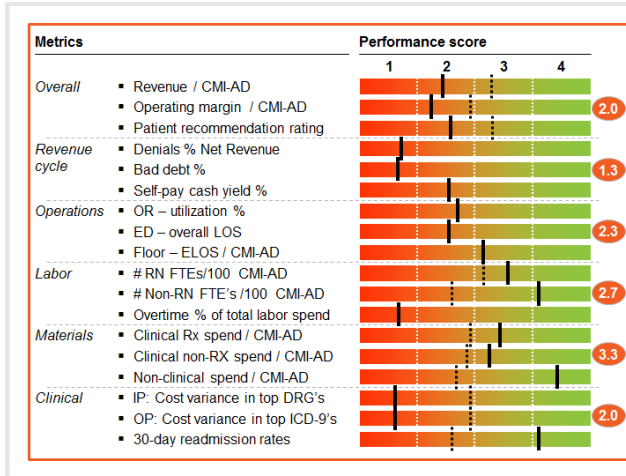


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Every hospital needs to understand its own performance across Operating Margin levers, relative to benchmarks and peers



Top level view – employing simple well-designed dashboards and benchmarks to identify areas of opportunity

- Overall performance
- Areas to investigate further
- Sense for scale of opportunity

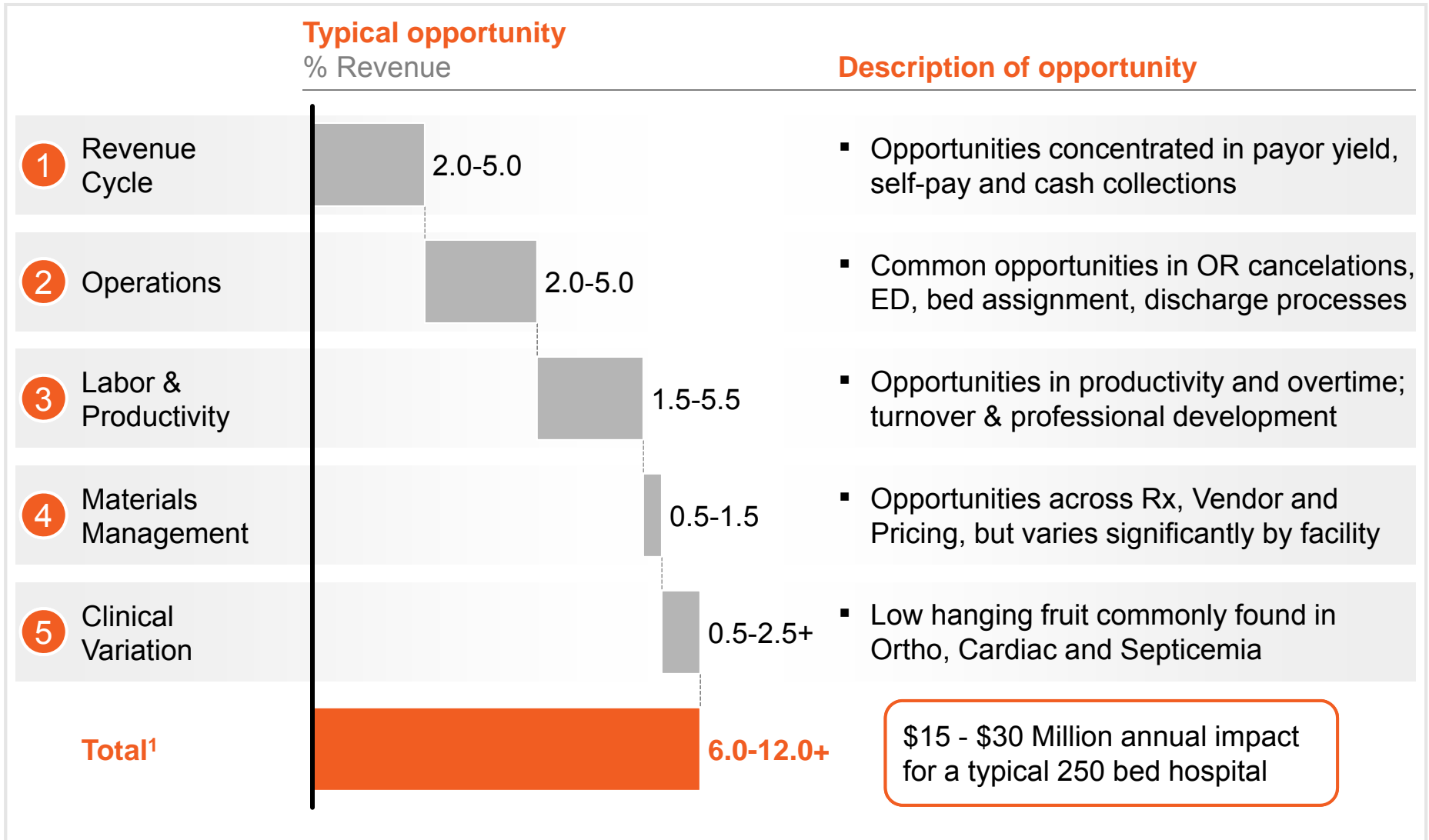


Detailed assessment – a rigorous effort to help in identifying, exploring and sizing issues and initiatives

- Time limited vs. on-going
- Cross-functional vs. topic-focused
- Tied to budget vs. project-based



Assessments generally identify significant opportunities, even in traditional areas

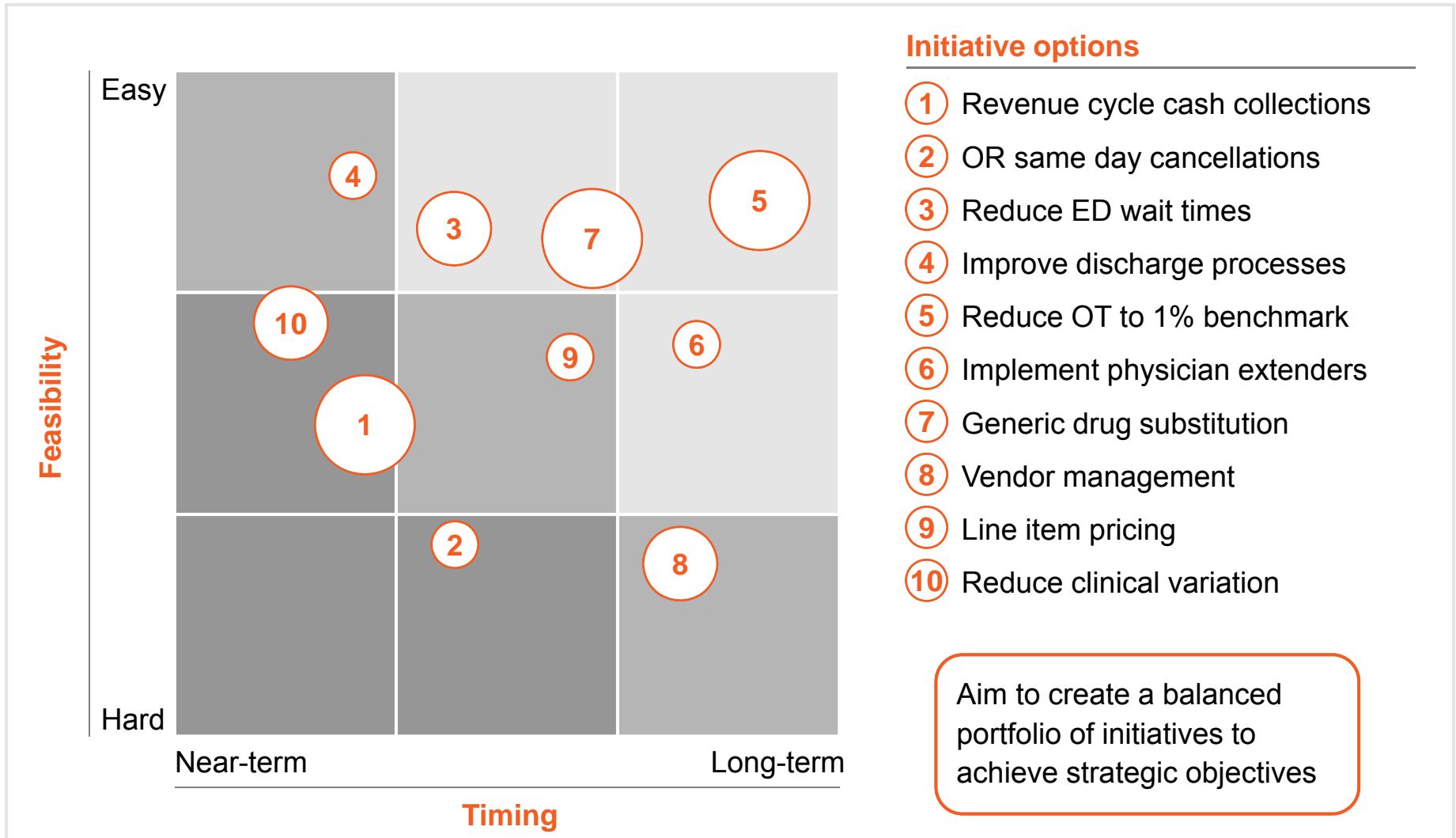


1 Not summative

Joint senior leadership prioritization of initiatives and targets is important to the creation of an integrated plan

ILLUSTRATIVE

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○ \$\$\$



Providers will need to move quickly over the next two years in order to seize opportunities



Next 12-18 months critical

- Many have been slow off the mark...
 - Evaluate the **impact of long-term trends** on your facilities
 - Understand your current **performance and opportunities**



Double down on core areas

- **Productivity and cost control** efforts critical to economic viability
 - Establish a burning platform for change
 - Prioritize and focus efforts in core areas
 - Track improvements and intervene early



Align to emerging patient segments

- **Target growth** to profitable and fast growing segments
 - **Identify and select** emerging segments and populations
 - **Sharpen value proposition** to meet different customer needs



Partner and innovate

- **Explore partnerships** with providers, payors, distributors, suppliers to improve quality, increase efficiency and reduce waste
 - **Build scale** to support innovation in care delivery model
 - Prepare for **population health** management

Q & A

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