



Developing a Hospital's Fiscal Strategy in an Era of Reform

The Issue

Hospitals should develop strategies around four forces that will affect their financial performance in the next five to 10 years.

Background

Hospitals and health systems will face a variety of financial challenges over the next decade, including pressures related to the economy, healthcare reform, and increased demand for care. Addressing these challenges will require, at a minimum, an understanding of the costs associated with care delivery. It also will require that healthcare organizations develop an ability to *control*—rather than simply *understand*—their costs.

Hospitals and health systems will need to conduct more in-depth analyses of the cost implications of care processes and delivery than most have done to date. In particular, they will need to concentrate on four forces that will affect their future costs:

- The impact of demographic changes on the Medicare Trust Fund
- Medicare spending patterns
- Morbidity in the non-Medicare population
- The complex nature of the healthcare market

Action Steps for Providers

Hospital and health system leaders should take the following steps in developing a fiscal strategy that will lead their organizations through the challenges of the next decade.

Summary of
"Fiscal Strategy
in an Era of Reform"
by David W. Young,
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Develop the ability to control—rather than simply understand—the organization's costs. There are only five drivers of an organization's healthcare costs: case mix, volume, resources used per case, cost of a resource unit, and fixed costs. Unless hospital leaders and physicians have a good understanding of their costs—and unless they design good systems to *control* their costs—they will be at the mercy of entities higher up in the healthcare food chain.

One of the most dramatic efforts to address resources per case was made in Grand Junction, Colo., where leadership by the primary care community resulted in a “culture” of incentives for cost control—a culture that was reinforced by withholding 15 percent of fees from physicians to create a risk pool managed by the Mesa County Physicians Independent Practice Association. When a physician's costs were kept low, the physician received the withheld fees at the end of the year, which provided an incentive for cost containment.

To better control resources per case, the Grand Junction primary care physicians gathered data on the cost profiles of specialists and reduced their referrals to those who were high-resource utilizers. Primary care physicians also led the way toward the regionalization of services and support “robust” (and lower-cost) end-of-life care, with an emphasis on hospice services rather than inpatient hospital care.

The results were impressive: Grand Junction saw a reduction in high-cost surgical interventions (with CABG and inpatient coronary angiography rates dropping to 60 and 55 percent of the Medicare national average, respectively), and a decrease in inpatient days during the last two years of life to 61 percent of the national average (with hospice days rising to 174 percent above the national average and deaths in hospitals declining to half the national average).

Ensure that senior managers and line managers throughout a healthcare organization are solidly behind—and deeply involved in—the organization's cost-control efforts. Controlling costs in hospitals and health systems requires the involvement of managers at all levels in the organization. Healthcare accounting professionals can be helpful in establishing transfer prices, designing a budget formulation process that relies on the five cost drivers discussed here, and preparing analyses of variances from the budget using these same cost drivers. However, both senior managers and line managers throughout the organization need to be solidly behind—and deeply involved in—the organization's cost-control efforts.

Heavily engage physicians in cost control. Physicians are the only ones who can both establish clinical pathways and monitor their colleagues' use of them.

For more information, read the full article on this topic: hfma.org/january2013bev1.