Could your organization survive if Medicare was your best payer?

Achieving Medicare profitability through strategic decision-making

Health system leaders have worried for years that reimbursement rates for all payers will ultimately fall to Medicare levels. For now, better payers balance the lower payments received from Medicare, and this cost-shifting has kept most providers in the black.

But healthcare reform is revolutionizing the payment model to include penalties for poor quality, bundled payments, and at-risk capitation reimbursement. Providers must strengthen their performance to be profitable at Medicare reimbursement rates.

What will it take to survive on Medicare rates in your organization? Most executives will need to reduce expenses by 20% to 30% to break even. Sounds daunting, but there are tested, reliable ways to get there.

"Providers need to implement significant organizational and operational improvements to become profitable under Medicare rates," says George Whetsell, a managing partner at Prism Healthcare Partners who specializes in hospital performance improvement.

Achieving a 20% to 30% cost reduction will require comprehensive planning and skillful implementation. Three areas stand out as vital.

REDUCING LABOR AND NON-LABOR COSTS

Labor represents 50% to 60% of a hospital's expense, so savings need to start here. According to Whetsell, the best way to gain labor efficiencies is by redesigning work methods and processes, especially in patient and clinical services.

Mukesh Gangwal, managing partner at Prism, agrees, noting there is 40% overcapacity in U.S. hospitals. Right-sizing staffing levels and non-labor expenses, such as medical supplies, to match capacity can yield huge savings.

"Those who have achieved Medicare profitability have reduced labor costs by streamlining overhead, simplifying management layers, and boosting centralization and standardization," says Brad Fetters, a managing partner at Prism who specializes in workforce consulting.

Still, there are limits to the gains that can be achieved in traditional areas, whether it's streamlining the maintenance department or finding a lower price on bed linens. You won't get the needed 20% to 30% solely through labor and non-labor cuts.

"Long-term success is rooted in regularly modeling your financial position based on Medicare and reviewing it with leadership."

Brad Fetters
Managing Partner
Prism Healthcare Partners LTD

CLINICAL PERFORMANCE

Once you mobilize your medical staff, you can confront care variation, a frequently untapped source of savings.

"Unlocking and then leveraging clinical expertise is the key to both improving quality and safety for patients—and, of course, achieving the corresponding cost savings," says Doug Monroe, MD, a Prism director. "We can take a recalcitrant medical staff and make them enthusiastic partners in risk mitigation. Physicians should be leading these efforts, not avoiding them."

And when you improve any clinical area, whether it's length of stay or care variation, that creates capacity, Monroe says.

That's the same excess capacity that Gangwal talks about, and it brings important new opportunities.

"You can only wrestle so much efficiency from the same old structure," Gangwal says. "At some point, you have to change the structure."

SERVICE LINE RATIONALIZATION AND RIGHT-SIZING

Your organization can't offer every service line. This is a startling realization for many providers whose longstanding culture dictates they do everything for their patients. "You must ask yourself: Should you be in transplants? Pediatrics? Oncology?" Fetters says.

Service line rationalization doesn't require you to close every service that's unprofitable, but it does require making difficult choices.

"This process requires significant physician integration, alignment, and leadership. Organizations that have this are able to achieve not single-digit reductions in costs, but double-digit," Fetters says.

Service line rationalization has a downstream effect on operations, of course. And that means a chance for right-sizing to fit the new market reality.

The Yakima Valley Medical Center in Washington is Medicare-profitable, says CEO Russ Myers, a Prism client. The hospital serves a low-income community dominated by Medicaid and Medicare patients. It maintains margins by defining its costs according to service line, and comparing that data directly to Medicare and Medicaid reimbursement rates. "Based on that data, we've been able to make cost adjustments in certain service lines, primarily cardiac, orthopedics, oncology, and neurosurgery," Myers says.

Likewise, Carson City Hospital in rural Michigan is Medicare-profitable, getting there in less than two years by reducing staff, closing its mental health program and working with 25 other hospitals to increase state reimbursement for OB patients, among other strategies. "I advise other hospital leaders to get aggressive in implementing change," says CEO Matt Thompson, also a Prism client. "Find an experienced partner with expertise and credibility, and be ready to accept their recommendations."

While data makes strategic decisions possible, it's also important to have the right experts who know how to interpret it and make it work to a hospital's advantage.

The road to Medicare profitability is not easy, but it is less rocky for leaders who are committed to making smart strategic decisions. "Long-term success is rooted in regularly modeling your financial position based on Medicare and reviewing it with leadership," Fetters says. "If you're not profitable there, you eventually will not exist."

Prism Healthcare Partners LTD is a national healthcare consulting firm focused exclusively on helping hospitals, health systems and academic medical centers improve their financial, operational and clinical performance so that they can better serve the needs of their communities. Prism's team of senior level healthcare consulting leaders have decades of experience working with clients to improve performance in six key areas: non-labor, workforce, revenue, clinical transformation, physician operations, and strategy. For more information call 312.610.4850 or visit www.prismhealthcare.com.

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