

THEME

Applying Best Practices in Healthcare Delivery

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INSIGHTS

Far-reaching decisions without reaching far.

Lowering Major Non-Salary Expenses Through Cost Management and Supply Chain Management Techniques

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About the Presenter

Steven Berger is President of Healthcare Insights, LLC, which specializes in the teaching and consulting of healthcare financial management issues. In addition, Healthcare Insights has developed INSIGHTS, the industry leading management accountability and decision support software solution for the healthcare industry. Prior to his role at Healthcare Insights, Mr. Berger was Vice President, Finance for seven years at 250- bed Highland Park Hospital in suburban Chicago, Illinois. Before Highland Park Hospital and since 1978, he has been a hospital or health system finance officer in New York, New Jersey and Missouri.

Mr. Berger has over 30 years of healthcare financial management experience. He holds a Bachelors of Science degree in History and a Master of Science in Accounting from the State University of New York at Binghamton. He is a CPA, a Fellow of the Healthcare Financial Management Association (HFMA) where he has served as President of the First Illinois Chapter. Mr. Berger also served a three-year term on the HFMA's National Board of Examiners and has also served as the Regional Executive of Region 7 of the HFMA. He is also a Fellow of the American College of Healthcare Executives (FACHE).

In addition, over the past several years he has presented many healthcare finance related seminars throughout the United States and Canada including several two-day classes such as Fundamentals of Healthcare Financial Management, Turning Data into Useful Information and Hospital Financial Management for the Non-Financial Manager and The Zen of Budgeting. He has also written several articles on healthcare financial and general management that were published in Healthcare Financial Management magazine, including an August 2004 Award Winning article on the Ten Ways to Improve Cost Management in Hospital, and the February 2007 Award Winning article, Treating Technology as a Luxury” Ten Necessary Tools.

Additionally, Mr. Berger is the author of “Fundamentals of Healthcare Financial Management,” originally published in 1999 by McGraw-Hill and the HFMA. This book was written from a practitioners point of view and is a distillation of Mr. Berger's many years on the inside of healthcare institutions. The third edition of the book was published in January 2008 and is available at www.josseybass.com. Additionally, Mr. Berger co-authored the 2002 text, “HFMA's Introduction to Hospital Accounting, 4th edition”, published by Kendall Hunt, available at www.hfma.org. Mr. Berger's has also written, “Understanding Nonprofit Financial Statements”. The third edition was just published in March 2008 by BoardSource and is available at www.boardsource.org. Finally, Mr. Berger's 2005 book, “The Power of Financial and Clinical Metrics: Achieving Superior Results in Your Hospital” is available at www.ache.org

Class Objectives

- Present the reasons why there is a great need and opportunity to reduce non-salary expenses
- Expose the need to manage for increased accountability in the hospital setting
- Identify specific areas of opportunity for rational supply chain expense reductions

Hospital Supply Chain Staff Face Challenges in Unstable Economy

- Some manufacturers selling products to hospitals are projecting price decreases in the next six months, while others suggest increases of up to 20 percent, according to a new analysis by the Premier healthcare alliance.
- Premier released its Economic Outlook and Inflation Estimates analysis through August 2009 on **March 30, 2009**. The report suggests that current economic conditions are making the financial decisions of not-for-profit hospitals more difficult than ever before.
- Eugene Schneller, and Natalia Wilson, MD, co-directors of the Health Sector Supply Chain Research Consortium at Arizona State University's School of Health Management and Policy, wrote the report's introduction about "How hospitals can cope with the sick economy."
- They noted that "Maximizing the dollar will require close collaboration between the hospital, the medical staff, the group purchasing organization and the supplier. Now more than ever, supply chain executives will be critical in leading initiatives to provide organizational sustainability."
- The Health Sector Supply Chain Research Consortium works to develop the best supply chain solutions to advance excellence in healthcare supply chain practice.

Hospital Supply Chain Staff Face Challenges in Unstable Economy

- The inflation estimates in the Premier analysis are by category, including cardiovascular services, clinical laboratory, facilities, foodservice, housekeeping, imaging, IT/telecommunications, nursing, pharmacy, support services, surgical services, and women and children.
- "Today's economic conditions are making not-for-profit hospitals' already difficult financial situation worse," said Mike Alkire, president of Premier Purchasing Partners. "Our analysis will help alert our members to market forces that could drive price changes in the coming months and years."
- Alkire said the keys to practical spending in this type of economy include: identification of opportunities; access to credible and current data; a working relationship with the physician community; open communication with suppliers with a goal of making them part of the solution; and optimization of group purchasing organization relationships.
- James Oliver, president and CEO of Yankee Alliance Inc., noted in the report that "one of the biggest challenges we face is competing for the limited amount of time our members have to address the opportunities available to save money."
- "There are numerous opportunities to reduce costs," Oliver wrote. "The challenge is prioritizing those opportunities and making time for the staff to convert products or work through the value analysis process, along with the many other pressures our members are facing."
- The Economic Outlook and Inflation Estimates, formerly called Inflationary Indices, is designed to help Premier members with budgeting. Premier publishes the report twice a year in the first and third quarter.
- Premier is a group purchasing organization working with more than 2,100 U.S. hospitals and 54,000-plus other healthcare sites.

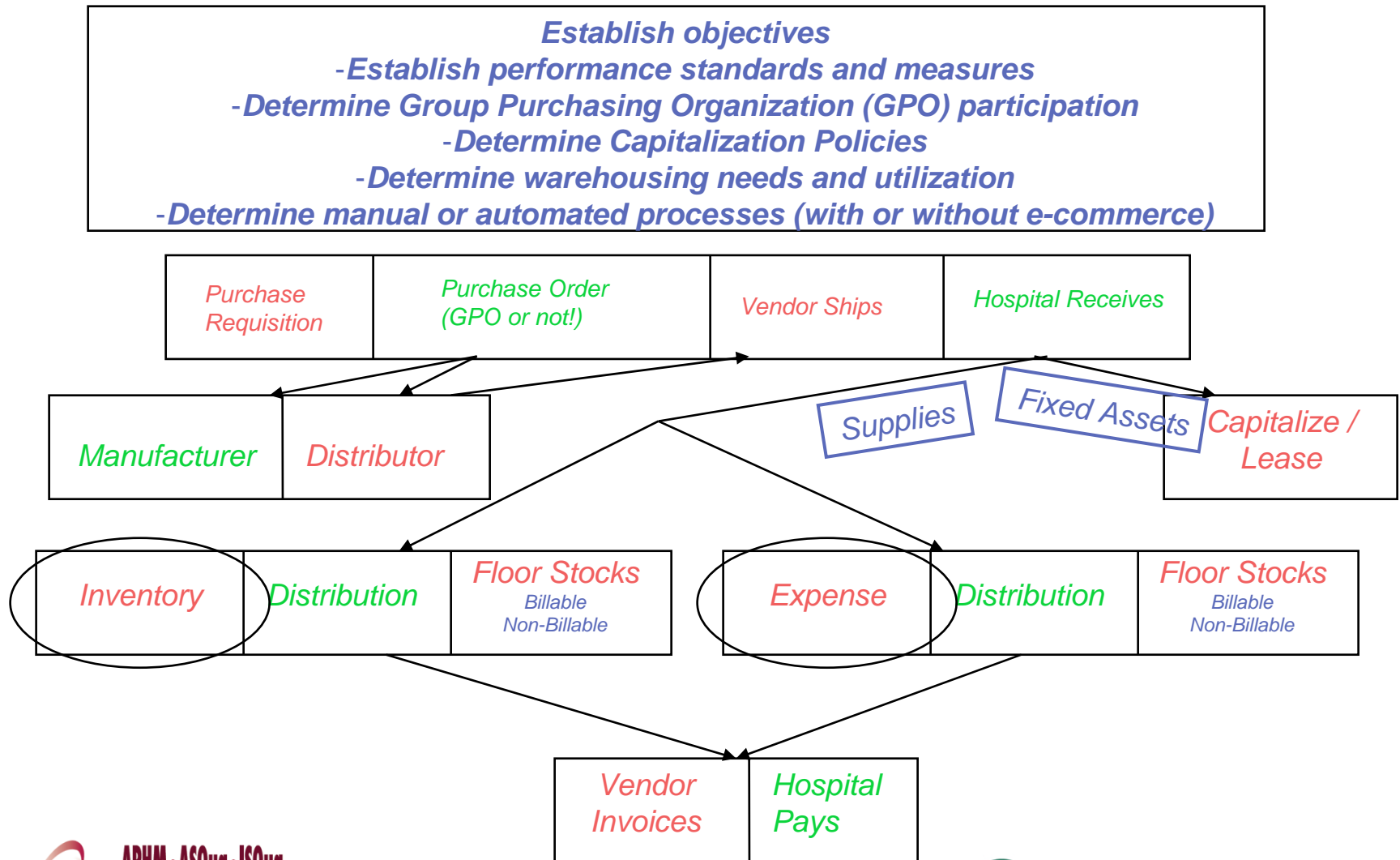
Supply Chain Management

- Management of the supply chain offers a significant opportunity to reduce expenses
- It is another area where improved profitability can be achieved through
 - overall process improvement and
 - departmental action

Supply Chain Management Cycle Overview



What Are Elements of The Supply Chain?



Supply Chain Manager Responsibilities

- Responsibilities Include:
 - Purchasing
 - Best prices
 - Best quality
 - Receiving Dock
 - Cost efficient
 - Accurate recording of received goods
 - Immediate distribution to floors
 - Storeroom/Warehousing
 - Inventory management
 - Distribution to floors
 - Medical supplies
 - Equipment
 - Revenue and charge tracking
 - Sterile processing
 - Including case cart (complete or limited processing)
 - Capital
 - Examines, develops, and manages data to support the overall capital process commensurate with current procedures and requirements
 - Provides full, up to the moment, capital data as required by the Vice President of Finance (CFO) and suggests revisions to capital processes as necessary given evolving capital needs and reporting requirements.

Additional Responsibilities

- Value Analysis Committee chair
 - (assigned to review specific items and GPO issues)
 - Surgical Subcommittee
 - Medical Supply Subcommittee

Which Departments Are Involved in the Supply Chain?

- Purchasing
- Receiving
- Warehousing (Storeroom)
- Sterile Processing
- Facilities Management
- Accounts Payable, and
- Every hospital department and...their staffs

The Supply Chain Cycle



Establish Objectives

- What value and benefits does the organization want to achieve through supply chain management?
 - Process efficiency
 - Improved cost management
 - Cost minimization
 - Cost reduction
 - Reduced resource consumption
 - Physician utilization
 - Staff utilization

Establish Performance Standards and Measures

- Performance standards and measures must be set and established by the hospital in order to know what to achieve
- These standards should be set based on
 - historical performance, and
 - peer percentiles (benchmarks)
- Appropriate standards for supply chain include:
 - Supply cost per adjusted admission (or adjusted per patient day)
 - Hospital wide
 - At the individual department levels

Determine Group Purchasing Organization (GPO) Participation

- GPOs are organizations that allow hospital to consolidate their purchasing power with other hospitals in order to
 - Lower prices through the leverage of volume purchases
 - Gain easier access to goods and services, including e-commerce
- The hospital needs to determine if it wants to participate with any of the various GPOs out in the industry, to gain this leverage.
- There are a number of specific requirements, such as purchase volumes and percentage of compliance of purchases with the GPO, that hospitals will need to follow, if they choose to align with a GPO
- The primary GPOs at this time are
 - Novation (VHA)
 - Premier
 - MedAssets
 - Amerinet

Determine Capitalization Policies

- Determine the two key elements of capital versus operating expense
 - Definition of Capital Budget Items would include all items
 - with a life of more than __ years, and
 - With a cost of \$_____
- Definition of Operating Expense Items
 - Everything else...
- These definitions are important in the supply chain because of the responsibilities of the supply chain manager in the expense versus capital purchasing

Determine Warehousing Needs and Utilization

- Warehousing versus Just-In-Time Concepts
 - Warehousing typically involves
 - An external building that is being used to store large quantities of inventories represented by
 - Medical supplies
 - Office supplies
 - A large internal storeroom be used to store large quantities of inventories
 - Just-In-Time typically involves
 - Turning over the inventory management to an organization that specializes in this area. Organizations with this expertise are
 - Suppliers, and
 - Distributors
 - The JIT companies delivering goods to the hospital on a accelerated basis, perhaps as much as daily.

Costs and Benefits of Warehousing Versus Just-In-Time

- *Costs*

- Warehousing
 - Holding cost of inventory
 - Shrinkage
 - Expired products
 - Staffing
 - Space
- Just-In-Time
 - Extra payments to the distributor for the inventory management and additional deliveries to the organization
 - Additional space in the receiving area (staging)

- *Benefits*

- Warehousing
 - Onsite access
 - Higher par levels yielding more assurance of availability
- Just-In-Time
 - Lower costs for inventory management
 - State of the art inventory management
 - More efficient processing of the supply chain

Determine Manual or Automated Processing (With or Without E-Commerce)

- The answer is easy
- In the 21st century, automated processing should always be the preferred option for most, if not all, process steps.
- E-commerce has the potential to improve supply chain management processes in all of the following areas
 - Pricing
 - Ordering
 - Shipping
 - Tracking, and
 - Billing (Invoicing)
- We will review the issues surrounding automation of the supply chain and e-commerce in detail, later in the class

Purchase Requisition

- Purchase requisitions are utilized by department managers to initiate the acquisition of non-stock items needed to operate the department
- Stock items are generally requisitioned automatically through restocking and par level analysis
- The purchase requisition includes all the pertinent information needed by the materials management department to place an order for the acquisition of the goods. These include
 - Vendor name
 - Product type
 - Product quantity
 - Product price (cost)
- The materials management department will then utilize the Purchase Requisition to issue a Purchase Order to the vendor

Purchase Orders

- Purchase orders are legally binding contracts
- It includes the general terms (Conditions of Purchase) between the buyer (hospital) and the seller (vendor)
 - Acceptance
 - Product warranty
 - Indemnity and insurance
 - Setoff
 - Termination
 - Compliance with laws
 - Controlling laws
 - Other
- The Conditions of Purchase can either be included as part of
 - Each individual purchase order, or
 - A controlling GPO agreement
- Purchase orders will be transmitted to the product manufacturer or distributor for processing, picking and shipping

Manufacturer

- Manufacturers actually design and produce the various products that are needed by the hospital to properly function
- These products may be directly clinical in nature or used by the hospital in overhead areas. They may consist of
 - Clinical supplies
 - Sutures
 - Bandages
 - Intravenous supplies
 - Clinical equipment
 - » Scalpels
 - » Instruments
 - Pharmaceuticals
 - » Prescription pills
 - » Prescription solutions
- The products may be disposable or reusable in nature
- The products may be packed by the carton, or as unit doses
- A hospital's supply list will run into the thousands of items
- Additionally, manufacturers may ship directly to the hospital after receipt of the PO or may ship to a distributor upon receipt of order

Distributor

- Distributors are companies that exist as middle-men between the manufacturer and the hospital provider of service
- Within the supply chain, distributors have become expert in the business of providing
 - logistics
 - transportation, and
 - inventory management services
- When used to optimize hospital costs and processes, distributors can be used to optimize inventory levels and costs throughout provider locations.
- This may be achieved through the adoption of Just In Time processing
- Another value added use of distributors involve their providing of product data in a form compatible with pricing information provided by the GPO and the manufacturers product specifications. Additionally, the distributor reports of the compliance percentage of GPO participation

Just In Time Inventory Management

- Traditionally, a hospital may have maintained its inventory within the four walls of the facility (or in an outside warehouse). In doing so, it bore the risks of:
 - Holding cost, for an indeterminate time
 - Increased opportunity for shrinkage
- JIT shifts the risks back to the distributor, because they now hold most, if not all, of the inventory back in their warehouse(s)
- Under JIT, the distributor will generally
 - Receive an automated message sent from the hospital floor. This message is sent when the par values have dropped to replacement levels, and
 - Ship the products in smaller units, appropriate to be sent directly to the floors JIT
- The caveats to adopting JIT are:
 - The supplier must be extremely reliable in its delivery schedule
 - The supplier must also have a reliable pipeline to obtain or manufacture the goods.
- The supplier should be able to charge slightly higher rates for this service and the risks it entails

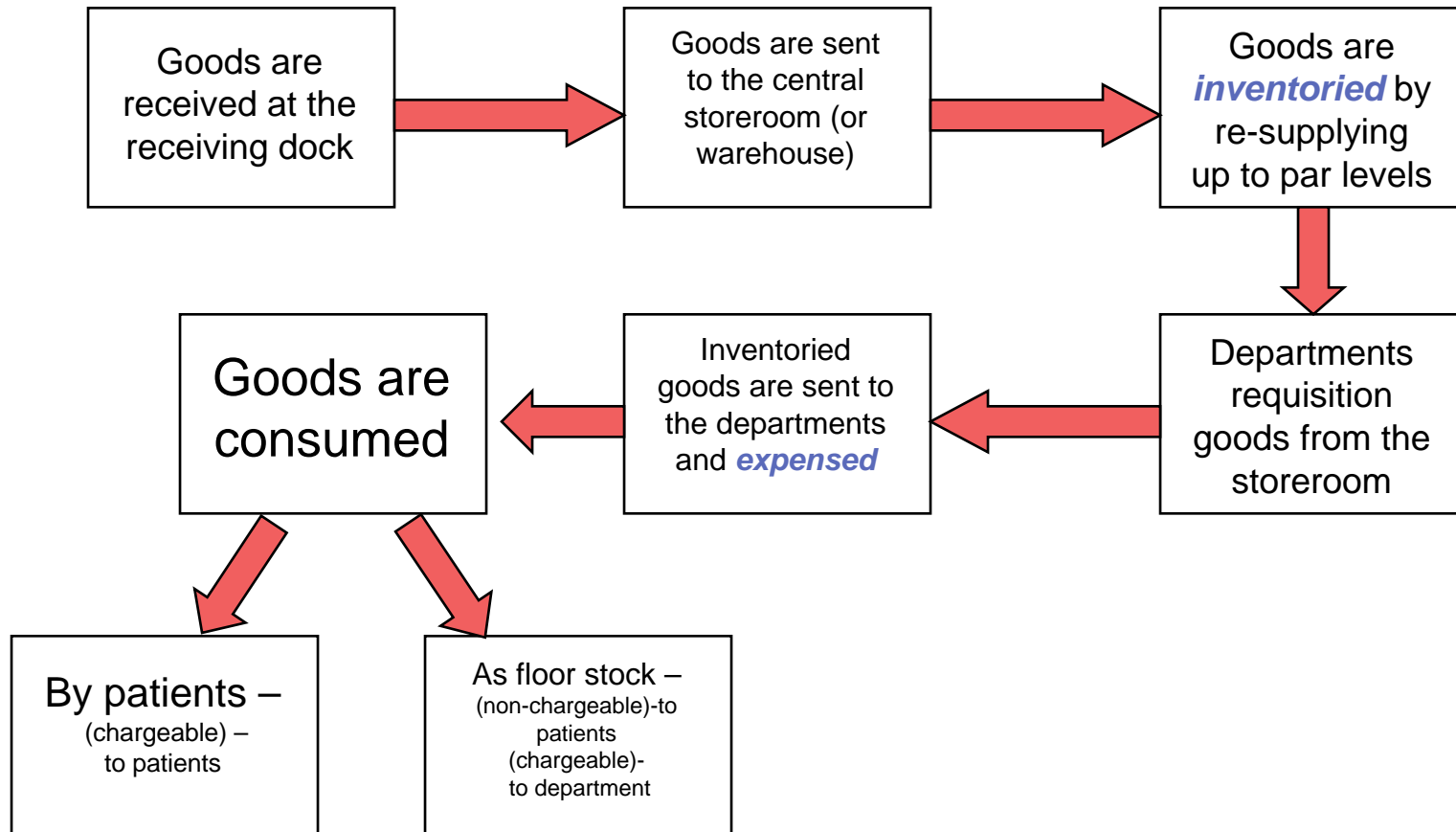
Vendor Ships

- Upon receipt of order, the manufacturer will
 - Place the order in its queue
 - Determine availability of items
 - Pick the items out of its existing inventory
 - Pack the items for delivery to the client
 - Prepare a delivery dock/receiving document
 - Ship the complete delivery
- A major issue in vendor shipping occurs when a specific item is not in stock at the time of order acceptance, picking and shipping
 - The vendor will place this item in “backorder”
 - “Backorders” can cause problems for the client when items not shipped, not received, are invoiced.
- Timeliness of order shipment is another item of concern
 - When orders are promised by a certain date, and reliance is placed by the hospital, it can become a problem for specific surgical or medical procedures that have been scheduled

Hospital Receives

- When the trucks roll up to the hospital's receiving dock, the dockworker signs for receipt of goods on behalf of the hospital
- This is an extremely important step in the supply chain cycle
- The receiving document should not list the quantity of line item products
 - This must be filled in by the hospital's receiver
 - It will be later be checked against the original purchase order and invoice to make sure all the items match
 - If there is a mismatch, then further analysis and communications must be held between the hospital and the vendor
- The goods are unloaded for further processing and delivery by the hospital

Here Is What Happens Next – Flow of Goods



Capitalize / Lease

- Determine if goods meet the capitalization policy
 - If not, continue with regular purchasing policies
 - If so, additional financial analysis may be required
 - See, for example, the MRI analysis on the next two pages
 - The organization needs a policy to for leasing, financing or outright purchase on capital items

MRI Analysis – Volumes

Ridgeland Heights Medical Center
Proforma of Proposed MRI Service
Financial and Volume Assumptions
July, 2009

CAPITAL COSTS:

Equipment (MRI)	\$1,750,000
Construction / Renovation	<u>250,000</u>
Total	<u>\$2,000,000</u>

USEFUL LIFE

5 years
5 years

VOLUMES:

	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	Total
Inpatient	350	371	393	417	442	1973
Outpatient	<u>1,610</u>	<u>1,707</u>	<u>1,809</u>	<u>1,918</u>	<u>2,033</u>	<u>9,076</u>
Total Volumes	<u>1,960</u>	<u>2,078</u>	<u>2,202</u>	<u>2,335</u>	<u>2,475</u>	<u>11,049</u>
Total Per Day	<u>8</u>	<u>8.48</u>	<u>8.99</u>	<u>9.53</u>	<u>10.1</u>	
Charge Per Test	<u>\$680</u>	<u>\$714</u>	<u>\$750</u>	<u>\$787</u>	<u>\$827</u>	

REVENUES:

Inpatient	238,000	264,894	294,632	328,256	365,333	\$1,491,115
Outpatient	<u>1,094,800</u>	<u>1,218,798</u>	<u>1,356,207</u>	<u>1,509,821</u>	<u>1,680,364</u>	<u>\$6,859,991</u>
Total Revenues	<u>\$1,332,800</u>	<u>\$1,483,692</u>	<u>\$1,650,839</u>	<u>\$1,838,077</u>	<u>\$2,045,697</u>	<u>\$8,351,105</u>

PAYOR MIX:

Medicare	34.20%	35.00%	35.50%	36.00%	37.00%
Medicaid	3.80%	4.00%	4.20%	4.40%	4.60%
Managed Care	26.80%	30.00%	33.00%	36.00%	39.00%
All Other	<u>35.20%</u>	<u>31.00%</u>	<u>27.30%</u>	<u>23.60%</u>	<u>19.40%</u>
Total Payer Mix	<u>100.00%</u>	<u>100.00%</u>	<u>100.00%</u>	<u>100.00%</u>	<u>100.00%</u>

CONTRACTUAL ALLOWANCES:

INPATIENT:

Medicare	100.00%	100.00%	100.00%	100.00%	100.00%
Medicaid	100.00%	100.00%	100.00%	100.00%	100.00%
Managed Care	20.00%	20.00%	20.00%	20.00%	20.00%
All Other	5.00%	5.00%	5.00%	5.00%	5.00%

OUTPATIENT:

Medicare	53.00%	53.00%	53.00%	53.00%	53.00%
Medicaid	80.00%	80.00%	80.00%	80.00%	80.00%
Managed Care	15.00%	15.00%	15.00%	15.00%	15.00%
All Other	5.00%	5.00%	5.00%	5.00%	5.00%

FREE CARE:

All Other:

Inpatient	0	0	0	0	0
Outpatient	10.00%	12.00%	14.00%	16.00%	18.00%

MRI Analysis - IRR

Ridgeland Heights Medical Center
Proposed MRI Service
Proforma Statement of Revenues and Expenses
July, 2009

	<u>2010</u>	<u>2011</u>	<u>2012</u>	<u>2013</u>	<u>2014</u>	<u>Total</u>
REVENUES:						
Gross Revenues	\$ 1,332,800	\$ 1,483,692	\$ 1,650,839	\$ 1,838,077	\$ 2,045,697	\$ 8,351,105
Less: Contractual Allowances	402,390	415,143	425,351	435,559	449,525	2,127,969
Less: Free Care Allowances	<u>38,537</u>	<u>45,339</u>	<u>51,834</u>	<u>57,011</u>	<u>58,678</u>	<u>251,400</u>
Net Revenues	<u>891,873</u>	<u>1,023,209</u>	<u>1,173,654</u>	<u>1,345,507</u>	<u>1,537,494</u>	<u>5,971,737</u>
EXPENSES:						
Variable Expenses:						
Salaries:						
2.0 Technicians	70,000	73,500	77,175	81,034	85,085	386,794
1.0 Clerical	<u>18,000</u>	<u>18,900</u>	<u>19,845</u>	<u>20,837</u>	<u>21,879</u>	<u>99,461</u>
Total salaries	<u>88,000</u>	<u>92,400</u>	<u>97,020</u>	<u>101,871</u>	<u>106,965</u>	<u>486,256</u>
Fringes @ 30%	26,400	27,720	29,106	30,561	32,089	145,877
Medical Supplies	82,320	91,622	101,975	113,499	126,324	515,740
Reduction of Ambulance cost	<u>(60,000)</u>	<u>(60,000)</u>	<u>(60,000)</u>	<u>(60,000)</u>	<u>(60,000)</u>	<u>(300,000)</u>
Total Variable Expense	<u>136,720</u>	<u>151,742</u>	<u>168,101</u>	<u>185,931</u>	<u>205,378</u>	<u>847,873</u>
Fixed Expenses:						
Cryogenes	23,000	35,000	36,750	38,588	40,517	173,854
Eq't. Maintenance Contracts	-	115,000	120,750	126,788	133,127	495,664
Utilities	40,000	42,000	44,100	46,305	48,620	221,025
Legal & Acctg (incl. billing)	20,000	21,000	22,050	23,153	24,310	110,513
Insurance	30,000	31,500	33,075	34,729	36,465	165,769
Office Supplies	5,000	5,250	5,513	5,788	6,078	27,628
Marketing	50,000	52,500	55,125	57,881	60,775	276,282
Facility Lease	96,665	101,498	106,573	111,902	117,497	534,135
Interest	-	-	-	-	-	-
Miscellaneous	<u>10,000</u>	<u>10,500</u>	<u>11,025</u>	<u>11,576</u>	<u>12,155</u>	<u>55,256</u>
Total Fixed Expense	<u>274,665</u>	<u>414,248</u>	<u>434,961</u>	<u>456,709</u>	<u>479,544</u>	<u>2,060,127</u>
TOTAL CASH OUTFLOWS	<u>411,385</u>	<u>565,990</u>	<u>603,062</u>	<u>642,640</u>	<u>684,922</u>	<u>2,907,999</u>
Net Cash Inflows / (Outflows)	<u>480,488</u>	<u>457,219</u>	<u>570,592</u>	<u>702,867</u>	<u>852,572</u>	<u>3,063,737</u>
Less: Depreciation Expense	<u>400,000</u>	<u>400,000</u>	<u>400,000</u>	<u>400,000</u>	<u>400,000</u>	<u>2,000,000</u>
Net Operating Profit / (Loss)	<u>80,488</u>	<u>57,219</u>	<u>170,592</u>	<u>302,867</u>	<u>452,572</u>	<u>1,063,737</u>
Internal Rate of Return						<u>14.32%</u>

Distribution to the Floor

- When the actual level of individual products in a department are reduced to the “restocking” level, requests are sent to the storeroom, warehouse or distributor, for replacement to the “par” level
 - Documenting the usage is a key element to the validity of the “restocking” and “par” levels
- The products, to be distributed, are
 - Picked in the warehouse
 - Recorded as being sent to individual departments, and
 - Transported to the floors (patient chargeable or non-chargeable)

Floor Stocks

- In a normal supply chain process, floor stocks are replenished when the actual level of individual products in a department are reduced to the “restocking” level in the inventory system
- At that point , requests can be sent automatically to the storeroom, warehouse or distributor, for replacement to the “par” level
 - As was previously stated, documenting the usage is a key element to the validity of the “restocking” and “par” levels. There are important issues surrounding the documentation
 - The staff must be trained to enter each product that is used into the manual or automated system. This records the transaction (usage), which also removes that product out of the inventory
 - The usage of the product should also be recorded in the medical record for medical necessity
- Billable vs non-billable
 - Each items ordered directly from the vendor or the storeroom either will or will not be billable (chargeable) to the patient.
 - It is important to have a policy so that all the documenters know whether an item is billable or not.
 - Many organization’s determine billable or non-billable by whether the item is necessary to provide patient care versus department convenience
 - If an item is billable, it is essential that the hospital have a system to capture all of them

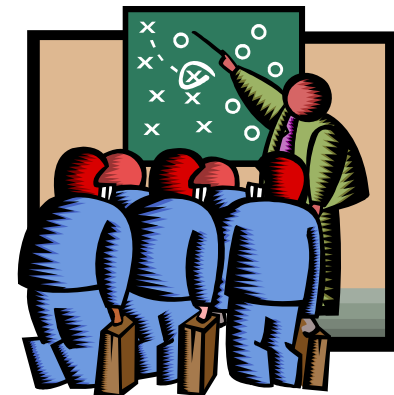
Vendor Invoices

- As part of the supply chain, the vendor will send out invoices for the products it has shipped and been received by the hospital
- The invoice should include an itemized list of the
 - Purchase order number(s)
 - products numbers
 - product names
 - Quantities of each product
 - Unit prices for each set of products
 - Extended price for each set of products (quantity x unit price)
 - Grand total of invoice
- The invoice should also include the payment terms
 - If no terms are stated, it is likely that standard terms apply (net 30)

Hospital Pays

- Upon receipt of the invoice, the hospital should initiate a “three way match” of
 - Purchase order
 - Receiving document
 - Invoice
- The elements of the invoice that need to match are
 - Price on the purchase order
 - Quantities on the receiving document
- If the price does not match, or is off by more than ____%, the invoice will not be paid. A notice will be sent to vendor for an adjustment
- If the quantities do not match, a notice will be sent to vendor for an adjustment
- Payment should be made within terms of the purchase order.
 - For example, net 30
 - Discounts should be taken if offered and the hospital has free cash to expend sooner.

Improvement Opportunities Within the Supply Chain



Improvement Opportunities

- Revenue Enhancements
 - Reduction in lost and late charges
 - Surgery
 - Charge based payers
 - Getting Supply Chain Management involved in managed care contracting
- Expense Reductions
 - Value Analysis Committee and process
 - Improved communications
 - Standardization through formulary and others usage
 - Accounts payable/purchasing audits

Improvement Opportunity Examples

Stillwater Medical Center – “You just have to identify a starting point and go.”

- Reduced expenses
 - Developed a *value analysis committee* – looking to find savings on items or services costing more than \$10,000 per year
 - Better pacemaker pricing and standardization
 - Give some responsibility to the Facilities Director,
 - » has no stake in the outcome
 - » Has to talk to everyone because starts from a lack of knowledge
 - Created an RFP for items or services over \$100,000
 - Value analysis committee recommendations and implementations saved the hospital \$926,000 in its first year
 - Currently working on Standardization throughout the hospital
- Increased revenue
 - Reviewed and found the weak links in the billing process that might
 - lead to lost revenue or
 - result in missed opportunities to capture more dollars
 - Followed supply charges from one point to the next
 - Were able to differentiate between billable and non-billable items
 - Ensured that charges were transferred accurately to billing

Value Analysis Product Request Form

VALUE ANALYSIS PRODUCT REQUEST FORM

Staff submitting and/or Value Analysis member signature:

Clinical
Surgical

Subcommittee Forwarded to _____

Product being introduced at Value Analysis by:

Department Name: _____

Item Requested: _____

Date of Request: _____

Date to submit to VA: _____

New Item Request: Y N Replacement Item: Y N If yes, Item Replacing: _____ ESI number: _____ Cost \$: _____

Justification for Request:

Date	Item Description	Vendor	Cost	Trial Y N	Area's	Start Date	End Date	Approved Y N	Other	Total

Information below is to be completed by Value Analysis Subcommittee:

Forward to Infection Control Y N Reason: _____

Forward to Hospital Value Analysis Group Y N Reason: _____

Forward to Safety Committee Y N Reason: _____

If Approved, implementation date: _____ If replacing current item, # of items on hand _____ Present Cost \$ _____ New ESI Number _____

Will current on hand inventory be used before new item put in service? Y N

Can items be returned to vendor/s? Y N If not, area to be charged for items _____

Inservice required for Product? Y N VA Members responsible for establishing inservice _____ Date: _____ Areas: _____

Approved by Value Analysis Chair _____ Rejected by Value Analysis Chair _____



Value Analysis Committee – Purpose and Policy

Purpose:

*The Value Analysis Committee will **establish and monitor** a process for the **timely, cost-effective, value-oriented acquisition** of needed supplies, materials and services.*

Policy:

1. Selection and acquisition of all product supplies and equipment must be coordinated through the Materials Management Department and the Medical and Surgical Sub Section Value Analysis Committees.
2. The Director of Materials Management has the authority to direct selection of most products through the Value Analysis Committee; the Director may elect to work directly with sub committee and/or the using department if indicated.
3. Recommendations to add products and/or change vendors must be submitted a request utilizing the **“Request for Product Review/Value Analysis Worksheet”** to the Director of Materials Management who will review the worksheet and forward to the appropriate committee for review.
4. Products recommended for trial will be coordinated by designated personnel, with the assistance of a designated Materials Management Buyer.

Value Analysis Committee – Product Introduction

Product Introduction:

1. *Internal.* Any member can introduce a new product or bring a product currently in use before the Sub Section Value Analysis Committee for review by requesting a Committee Leader to place it on the agenda for the next meeting once a request form is filled out and submitted.
2. Once the request form has been reviewed by the Director of Materials Management and/or Designee it will be forwarded to the proper sub committee for analysis. Anyone on the hospital staff can bring new products, product changes, and/or complaints about products to the Sub Committee Leader or a member of the Value Analysis Committee. *Physician requests for evaluation and trial of a new product are handled in the same manner.*
3. *External.* Representatives of suppliers who wish to introduce their product to the hospital must **first** present it to the Materials Management Department. If the product merits further investigation, the Materials Management Department will refer it to the Sub Committee Leader. The Sub Committee Leader will refer the item to the committee for consensus of opinion on the merits of the product.
4. A “Request for Product Review/Value Analysis Worksheet” form should be returned by sub committee leader to the Value Analysis Committee for final approval. Implementation of product will be arranged with Sub Committee Leader and a Materials Management Buyer.

Value Analysis Committee – Product Survey

Product Survey:

Once the sub section committee has completed the evaluation and cost analysis , the Hospital Value Analysis Committee will:

1. Provide a point of entry and an arena for the consideration of new expenditures to be incurred by the hospital based upon the following criteria:
 - a) Any product, equipment, or service that requires the purchase of a disposable component.
 - b) Any product or purchased service that represents an annual expenditure in excess of: _____.
 - c) Any product that, in the opinion of the Director of Materials Management, or the Sub Committee Leader, may underline the efforts of standardization within the hospital.
 - d) Any current contracted commitments of the hospital.
2. Provide a forum to monitor and summarize accomplishments and cost-effective practices within departments of the hospital.
3. Investigate and, where feasible, standardize when two or more products are used to perform the same function.
4. Ensure the use of a Product Evaluation Request form be utilized when tracking a product trial.
5. Review product usage so its economic impact can be identified and evaluated as necessary.
6. Reduce the number of different brands of essentially identical products.
7. Monitor and evaluate the use of disposable and re-usable products.
8. Review cost analysis studies prior to deciding whether a product should be assembled in-house or purchased pre-assembled.
9. Review the use of current products to project and verify continued cost-effectiveness into the future (long-range analysis)
10. Approve all new inventory items and deletions form the Store-room (deletions to be reviewed at least quarterly).
11. Enlist experts to assist in the evaluation of items for specialized units within the hospital.
12. Assist with the analysis of patient charges, when so requested by the CFO and/or Patient Accounting CDM Manager.
13. Materials Management will be responsible for requesting product samples, while working with the Sub Section VAC
14. At the conclusion of each trial, the sub committee team leader will submit a completed *Request For Product Review/Value Analysis Worksheet* to the Hospital Value Analysis Committee for documentation and review.
15. As part of the product evaluation process, the Value Analysis Committee, with the guidance from Materials Management, must allow for disposition of “old” product stock.

Value Analysis Committee – Product Survey (continued)

16. All products will be evaluated based on the following criteria:

- Quality
- Safety
- Effectiveness
- Disposable vs. Reusable
- Ease of Storage / Appropriateness for Storage
- Price
- Availability
- Delivery Time Duration
- In-service Support
- Servicing and Repair
- Other Hospital User Experience
- Competitive Product Comparison
- Independent or company Studies
- Recommendations from Physician / Hospital Staff
- Environmental Impact
- Durability
- Ease of Use / Operation
- Any Other Special Considerations

17. Prior to a trial, the assigned subcommittee must establish specific criteria for each product authorized for trial. In addition, staff should process all samples / supplies used during trials as patient charge items, unless otherwise directed by the VAC.

18. The committee member who requests a product review, or the member(s) assigned by the Sub Committee Leader shall be responsible for managing feedback data. This member is then responsible for presenting a report to the full committee, for either approval or disapproval of the product. If the committee recommends disapproval, the alternatives are:

- Continue using the current product and/or procedures.
- Re-evaluate the need for change.
- Extend the trial evaluation time.
- Review other products.

The selection of appropriate action is the responsibility of the full Value Analysis Committee and then it is directed back to the specific member concerned. When a product is approved, the ordering process must be coordinated through Materials Management prior to vendor notification. At this time patient accounting should be involved to determine if a item is chargeable, if so that a CDM as been assigned before item is put in service, to insure that all revenues are captured.

EXCEPTIONS: Emergency situations will be handled on a case by case basis with the needs of our customers coming first.

Follow-up and evaluation may be done depending upon the specifics of any given emergency product/service procurement.



Improvement Opportunity Examples

Lakeland Regional Medical Center —“You need to have a plan and gain trust in some way.”

- Reduced expenses
 - Nurse hired by Materials Management
 - To better understand the clinical equipment and supply issues, and
 - Work directly with physicians on some physician preference items
 - Internally benchmarks the costs of physician doing same procedures, and disseminates the information to the physicians
 - Standardization
 - Respiratory product totaled 400. Found that only 180 were needed.
 - They reduced the number of product lines, and
 - Took advantage of better volume related discounts
 - Developed a Nonlabor Expense Reduction Team
 - Discusses and analyzes new products and existing service lines
 - Supply costs per adjusted admission decreased from
 - \$1,017 in base year to
 - \$ 947 in third year of program

Improvement Opportunity Examples

OhioHealth – “We found out physicians are most responsive when they have the information they need to make good decisions, and have several options to choose from.”

- Reduced expenses
 - Value Analysis Committee
 - Reengineered to focus on new technology
 - Coordinated effort amongst staff, including physicians who will submit requests through Medical Director
 - Evaluation will focus on
 - » System’s return on investment
 - » Improved clinical outcomes
 - » Impact an item will have on reimbursement
 - Standardization
 - Standardizing product utilization among physicians performing the same procedure
 - Two material clinical consultants, RNs, use their expertise to assist with analysis
 - Communications
 - MM and Finance routinely share data with individual hospitals via a report that details
 - Savings per service line
 - Opportunities for additional drug and supply savings, and
 - Total impact of contracted savings
 - Supply cost savings have been substantial over the past three years
 - \$ 7.1 million in Year 1
 - \$ 5.6 million in Year 2
 - \$ 8.4 million in Year 3

Does Your Hospital Use a Non-Salary Ratio to Develop its Initial Budget?

- Just like the Labor Ratio, there is a widely accepted ratio for Non-Salary expenses
- The ratio is
 - *Supply Expenses (excluding depreciation, interest and bad debts) / Total Revenues*
- Best sources suggest that hospitals are generally in the 16 – 19% range
 - But some investor-owned hospitals are running in the 12 – 13% range
- If you start your budgeting process with a ratio goal in mind, it will simplify the process

Statement of Operations

Ridgeland Heights Medical Center Statement of Operations

	<u>2008</u>	<u>2007</u>	Percentage Change
REVENUES:			
Inpatient Revenue	73,000	74,000	-1.35%
Outpatient Revenue	<u>72,000</u>	<u>69,000</u>	4.35%
Total Patient Revenue	<u>145,000</u>	<u>143,000</u>	1.40%
<i>Less:</i>			
Contractual and Other Adjustments	(49,000)	(48,000)	2.08%
Charity Care	<u>(2,600)</u>	<u>(2,200)</u>	18.18%
Net Patient Service Revenue	<u>93,400</u>	<u>92,800</u>	0.65%
<i>Add:</i>			
Premium Revenue	2,100	1,300	61.54%
Other Operating Income	<u>1,200</u>	<u>1,200</u>	0.00%
Total Revenue	<u>96,700</u>	<u>95,300</u>	1.47%
EXPENSES:			
Salaries	36,000	34,000	5.88%
Contract Labor	1,000	1,500	-33.33%
Fringe Benefits	<u>7,000</u>	<u>6,800</u>	2.94%
Total Salaries and Benefits	<u>44,000</u>	<u>42,300</u>	4.02%
Bad Debts	4,600	4,400	4.55%
Patient Care Supplies	15,500	15,000	3.33%
Professional and Management Fees	3,600	3,600	0.00%
Purchased Services	5,400	5,600	-3.57%
Operation of Plant (including utilities)	2,600	2,500	4.00%
Depreciation	11,000	10,500	4.76%
Interest & Financing Expenses	7,400	7,600	-2.63%
Other	<u>3,800</u>	<u>5,200</u>	-26.92%
Total Expenses	<u>97,900</u>	<u>96,700</u>	1.24%
Operation Margin	<u>(1,200)</u>	<u>(1,400)</u>	-14.29%
NON-OPERATING INCOME:			
Gain/(Loss) on investments	1,200	600	100.00%
Investment Income	<u>6,400</u>	<u>5,500</u>	16.36%
Total Non-Operating Income	<u>7,600</u>	<u>6,100</u>	24.59%
Net Income	<u>6,400</u>	<u>4,700</u>	36.17%

Ridgeland Heights Medical Center

For the 12 months ending

Non-Salary Expense Ratio 12/31/08

Supplies	15,500	<u>16.0%</u>
Purchased Services	5,400	
Professional and Management Fees	3,600	
Operation of Plant	<u>2,600</u>	
Total Non-Salary Expenses	27,100	
Total Revenues	<u>96,700</u>	
Non-Salary Expense Ratio	<u>28.0%</u>	

Supply Expense as a Percentage of Net Patient Revenues

EQUATIONS:

Supply costs divided by total revenues

EXAMPLE:

	<u>Supply Costs</u>	<u>Net Patient Revenues</u>	<u>Actual Percentage</u>	<u>Budget Percentage</u>	<u>Benchmark</u>
July, 2008	\$ 1,900,000	\$ 10,000,000	19.0%	18.0%	17.0%
August, 2008	\$ 1,800,000	\$ 9,000,000	20.0%	18.0%	17.0%
September, 2008	\$ 1,750,000	\$ 10,500,000	16.7%	18.0%	17.0%
October, 2008	\$ 1,800,000	\$ 10,000,000	18.0%	18.0%	17.0%

- This metric quantifies the total cost of supplies as a percentage of the net patient revenues recorded by the hospital. It can be used to determine the average supply costs percentage needed to operate the facility.
- The *lower* the number, the better.
- Benchmark information is available (from the Advisory Board) and general values are within the 16 - 18% range.

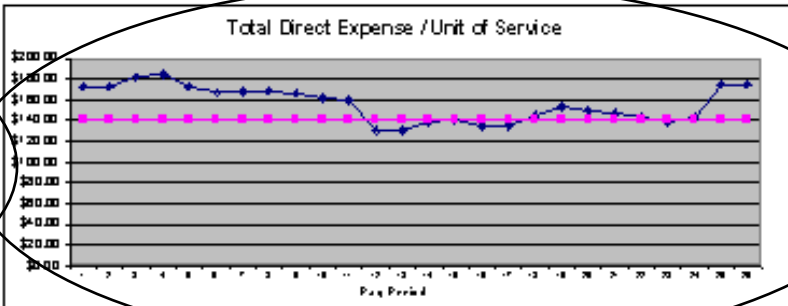
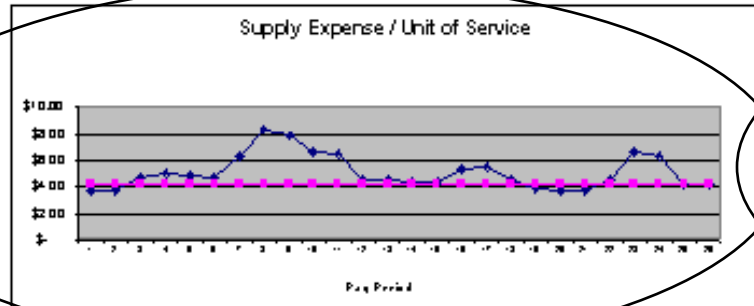
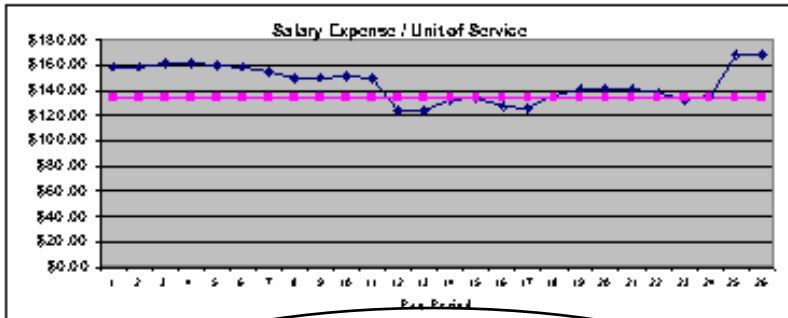
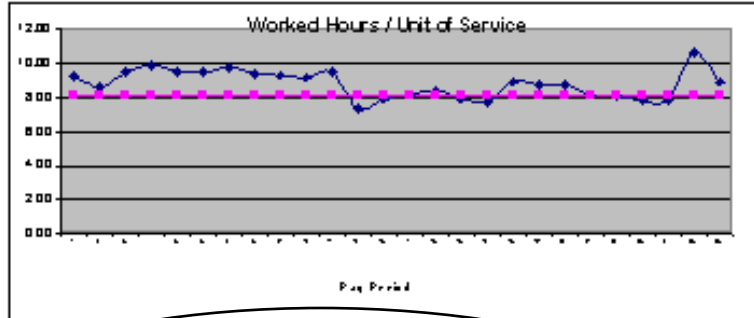
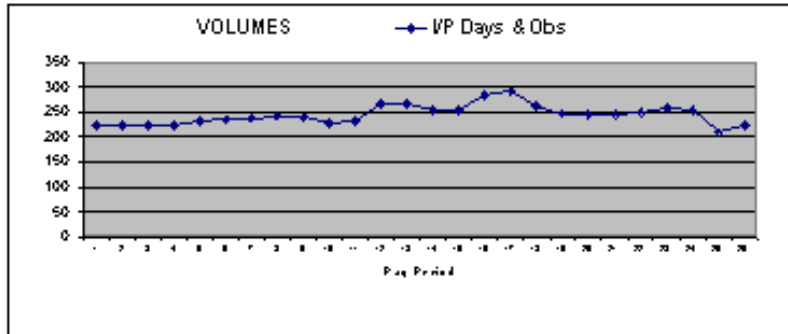
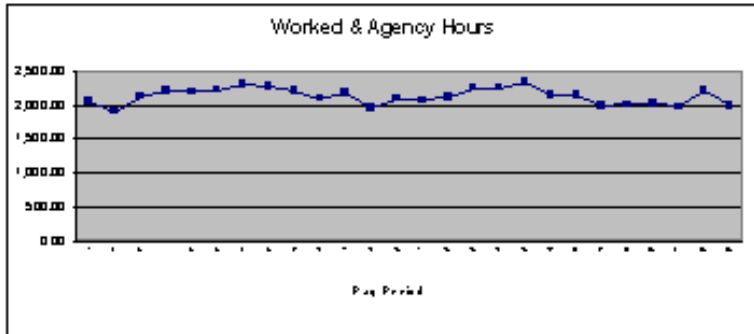
Supply Chain Metrics



Healthcare Insights, LLC

6140

HOSPITAL
CCU



Class Poll

1. Has your hospital mapped the Supply Chain to determine areas for specific improvements?
2. Have Supply Chain objectives been established at your hospital?
3. Are you using a large storeroom or warehouse or have you adopted Just In Time process?
4. Is your hospital fully operational across the entire Supply Chain with Electronic Supply Chain?

Case Study
Community Hospital
Midwest United States

Secrets from the Front

Supply Cost Reduction

Who: Community Medical Center
Midwest
Annual Supplies \$13 million

Problem: Declining
reimbursements force
continued need for cost
savings

Solution: Supply chain solutions
across the entity, both with
internal teams and two
external consultants
working in concert

Background. Over the past five years Hospital A had been very active in managing its nonlabor costs:

- Top performer in cmix adjusted nonlabor cost per adj discharge
- Hiring a consultant in 2002 to successfully reduce costs \$2M+
- Employing THREE nurses
- Joining an award winning regional GPO coalition in 2004
- Internal efforts saving \$1M+ in 2006

Approach. Strategic Sourcing Results was brought in by the CEO in 2007 and worked with Finance, Operations and Purchasing to achieve incremental savings.

Scope. Supplies and Purchased Services. \$750,000 was targeted to be implemented over 32 weeks, with only three hours per week from three directors required.

Results. Annual recurring savings of \$961,301 implemented and verified.

Project length: 8 months. Percentage savings from Vendor/ Product Change 4%: .

Supply Cost Reduction

Reduced Price:

Implants	\$362,000
Lab Regents, Ref Lab	\$135,000
Cath Lab	\$51,000

Lower Cost Alternatives:

Med/Surg	\$90,000
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Revenue Recovery: Implants	\$171,000
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Purchased Services: Reduced Costs	\$152,000
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TOTAL \$961,000

Medical / Surgical Lower Cost Alternatives

Analysis and Approach

Obtained PO Data Download then Sales History from Distributor. Out of 300+ manufacturers, and 2100+ items purchased, No major Gaps noted.

Based on Consultant experience, savings were believed to exist and achievable could be wrung with incentive alignment and resource support from the distributor. Offered a one year extension to the distributor contract if they were successful in bringing forward over savings exceeding 5% of their total sales

Results

Many areas were automatically implemented or trialed after Product Evaluation Committee review. Total Savings \$56,000 of \$90,000

- Reduced wrap usage by leasing containers \$7,000/yr
- Replaced higher cost electrodes in custom packs \$5,000/yr
- Replaced higher cost Clippers, Drains \$17,000/yr
- Standardized cautery, orthopedic soft goods \$19,000/yr
- Other: Ace bandages, gowns, cuffs \$8,000/yr

Revenue Recovery

High margin, physician preference, coding heavy procedures such as spinal implants typically carry support from manufacturers for billing review and consulting- pro bono- in lieu of offering higher discounts.

The service consists of reviewing patient records, then reviewing bills and payments to ensure maximum funds are received as justified by the documentation. This client had done a revenue project in the previous year.

Example savings - Neurostimulator implants:

- 24 implants reviewed, all had billing errors, 11 were recoverable retroactively and proactively for \$171,000
- 24 missed a programming service charge which Medicare pays at \$120
- 5 missed charges for the programmer implant
- 5 charging kits not passed through with a C code
- 6 generators or leads undercharged: Upcharge of 257% is manually calculated and not computed correctly on 25% of the bills. Four were (non- MC) recoverable

Purchased Services

Purchased Services are a very lucrative category of areas for savings. Savings tend to be a function of the control over cost drivers. Typically, these arrangements are too loosely controlled or contained arrangements which do not reflect Hospital incentives.

We recommend auditing these areas to identify contract compliance, risk/ reward incentives, cost controls, and competitiveness of rates quoted.

Example:

Security was staffed 3 officers per shift 24/7 at this client, which benchmarked high. Rates were competitive for the experience level, and the experience level provided certain productivity levels justifying a slight hourly upcharge.

Analysis showed three surprising facts which reduced labor 25%:

1. Up to .5 FTEs per shift were used to open doors due to lock outs. Engineering did not have master keys. The on call administrator and VP Facilities were given keys and incentives placed to reduced lock outs
2. Patient watches were performed by security, which could be performed by clinicians. However, investigation concluded doctors overused this description and were given a clinical pathway checklist which reduced watched 60%
3. Incident review by shift showed Tue and Wed nights were half as likely to have any event where security trained personnel were required. Staffing by event projections need was introduced

Supply Chain Savings- Scope Areas

General	Clinical Supplies	Purchased Services	Other
<ul style="list-style-type: none"> o Office Products o Forms o Copiers o Equipment Rentals o Freight o Postage o Furniture 	<ul style="list-style-type: none"> o PPI o Other Surgery o Med/ Surg o Other Cardiac o Lab o Diagnostic Imaging 	<ul style="list-style-type: none"> o Utilities o Telecommunications o Foodservice o Building Maintenance o Building Insurance o Transcription o Reference Lab o Linen* o Reprocessing o Temporary Labor o IT Services o Patient Transportation o DME o Dialysis o Outsourced Programs o Advertising o Storage o Fees and Subscriptions o Security o Landscaping o Cleaning Services o Travel, Ed and Books o Other 	<ul style="list-style-type: none"> o Revenue o RFID

Action Items

- Understand the elements of the supply chain so that informed decisions can be made
- Make a conscious and concerted effort to recognize the many areas of opportunities for supply chain cost improvements
- Use Supply Chain Metrics to set goals and monitor outcomes
- Involve your physicians in supply chain improvement efforts
 - Make sure appropriate and effective information is available
 - Be firm about achieving improvements
- Establish a Value Analysis committee if it currently does not exist
- Determine how to improve Value Analysis committee outcomes if one already exists

Conclusion

- There are untold millions of dollars being misspent within a hospital's supply chain
- Significant opportunities exist to reduce overall supply chain expenditures by up to 30%
- Identifying the most likely areas of cost reduction opportunities is not that difficult and needs to be undertaken by hospitals for good management purposes
- Enlisting the assistance of the physicians will be essential to maximizing reduction opportunities

Appendix

- List of onsite classes – by time
- List of onsite classes – by audience and time
- INSIGHTS decision support management accountability software features

List of Onsite Classes – by Time Frame

- **Two-day classes:**
 - Fundamentals of Healthcare Financial Management
 - Turning Data into Useful Information – *How to collect, analyze and report financial and clinical data to enhance decision-making in healthcare*
 - Managing the Modern Medical Center With Metrics – *Achieving superior financial and clinical results with intelligent information*
 - The Zen of Budgeting – *Simplifying the Process for Better Results*
 - Gaining Insight and Improving Key Hospital Processes – *Revenue Cycle and Supply Chain Management*
 - Hospital Financial Management for the Non-Financial Manager – Tips and Techniques to Ensure Your Success
 - Achieving Exceptional Leadership and Cost Management (day and one half)
- **One-day classes**
 - Any of the two-day classes listed above can be taught as one-day classes
- **Three-hour classes**
 - Improving the Oversight Function Within Your Hospital: *The Power of Financial Information for Decision Making*
 - Advanced Healthcare Financial Management – *What Every Healthcare Executive Should Know*
 - Financial and Clinical Benchmarking – *Knowing how you are doing compared to your peers...and why*
 - Inside the Mind of the Hospital CFO
 - Proven Cost Management Techniques That Save Real Money
 - Leading and Managing for Superior Results – **KEYNOTE ADDRESS**
- **90 Minute classes:**
 - Best Practices in Key Financial Metrics
 - Leading and Managing for Superior Results – **KEYNOTE ADDRESS**
 - Inside the Mind of the Hospital CFO
 - Overview of the Healthcare Industry and Healthcare Economics
 - The Value of Strategic Financial Planning in Healthcare Organizations
 - Proven Cost Management Techniques That Save Real Money
 - The Value of Productivity Management to the Healthcare Organization's Bottom Line
 - Evaluating the Role and Value of Cost Accounting in Healthcare

List of Onsite Classes – by Audience and Time

- **Board of Directors**
 - Improving the Oversight Function Within Your Hospital: The Power of Financial Information for Decision Making – **3 hour class**
 - Managing the Modern Medical Center With Metrics - **90 minute or 3 hour class**
 - The Value of Strategic Financial Planning in Healthcare Organizations - **90 minute class**
 - Leading and Managing for Superior Results - **90 minute class**
 - Best Practices in Key Financial Metrics –**90 minute class**
- **CEO, COO and Vice Presidents**
 - Turning Data into Useful Information – (should also include Financial and Non-Financial Managers) – **2 day class**
 - Managing the Modern Medical Center With Metrics - **90 minutes up to 2 days**
 - Proven Cost Management Techniques That Save Real Money – **3 hour class**
 - Advanced Healthcare Financial Management – *What Every Healthcare Executive Should Know* – **3 hour class**
 - Leading and Managing for Superior Results – **3 hour class**
 - Inside the Mind of the Hospital CFO - **3 hour class**
 - Evaluating the Role and Value of Cost Accounting in Healthcare - **90 minute class**
 - Best Practices in Key Financial Metrics –**90 minute class - New 2005**
- **Clinical and Operating Managers**
 - Hospital Financial Management for the Non-Financial Manager – **2 day class**
 - Turning Data into Useful Information - **2 day class**
- **Financial Managers and Staff**
 - The Zen of Budgeting – Simplifying the Process – **2 day class**
 - Fundamentals of Healthcare Financial Management - **2 day class**
 - Turning Data into Useful Information - **2 day class**
 - Managing the Modern Medical Center With Metrics - **90 minutes up to 2 days**
 - Evaluating the Role and Value of Cost Accounting in Healthcare - **90 minute class**
 - Best Practices in Key Financial Metrics –**90 minute class**
 - The Value of Productivity Management to the Healthcare Organization's Bottom Line - **90 minute class**

Check List of INSIGHTS Features

- Financial Modules (using parameters controls with alerts)
 - Detailed Income Statement, with hierarchical controls for system, company, executive, division and department
 - Electronic drilldowns
 - Labor Management drilldowns to job titles and personnel level
 - Non-labor expense drilldowns to accounts payable and journal entry
 - Balanced Scorecard / Dashboard (specific to your organization)
 - Financial and Operating Indicators
 - What-If Analysis
 - Productivity Monitoring (utilizing parameter controls with alerts)
 - Productivity reports and graphs
- Human Resources Module
 - FTE Position Control (linked with budget)
 - Job Coding Budgeting
- Flexible Operating Budgeting Module (utilizing Work Load Measurement Units)
 - Salaries
 - Revenue Projections
 - Direct Revenue and Expense
 - Goals
 - Standardized Budget Reports
- Dynamic Capital Budgeting Module
 - Criteria Based Capital Budgeting
 - Capital Request (approvals linked to operating budget through depreciation)
 - Capital Monitoring
- Project Management (develop templates to manage repeatable processes)
 - On-line real time reports specific to Hospital including financial statements and productivity reporting.
 - Flexible report writing by the Director of Decision Support and designated staff