Estimate of the Situation

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Structure and the Bottom Line

Genuine and potentially very significant opportunities to increase net revenue and reduce expenses are available for hospitals that act to reorganize business lines, realign reporting relationships, and rethink corporate structures. Current and projected revenue and expense trends have created a perfect storm that makes taking action critically important.

Background

The percentage of outpatient net revenue has been growing for decades. Among our clients, the averages range from about 50% in larger urban hospitals to 90% and more in small rural and critical access hospitals.

Unfortunately the outpatient revenue upon which hospitals depend is at risk for loss to a wide array of non-hospital providers. Competing for that revenue are diagnostic imaging centers, surgery centers, regional laboratories, outpatient rehab centers, urgent care centers, and rapidly developing retail walk-in clinics such as those operated by Walmart, Walgreens, and CVS. Retail walk-in clinics and free standing urgent care centers pose a direct threat to the physician practices that hospitals have been acquiring at top speed. The national shift of insurance premium costs from employers to employees, increased deductibles, and price transparency mandates create a competitive disadvantage for hospital-based services and accelerate the loss of primary care revenue.

Hospitals facing bottom line challenges can reduce expenses and increase net revenue by identifying and resolving existing structural issues.

Structural Factors Affecting Costs

- **Span of Control:** The hospital's organization chart should be based upon span-of-control principles. Executives and managers should be responsible for 6 to 8 key result areas. A span of control that is too wide will produce managerial burnout and inadequate resource management. A span of control that is too narrow will produce micromanagement and under-utilization of expensive management talent.
- **Bureaucracy Tiers:** There should be as few layers of management between the "top" and the "bottom" of the organization as possible. Too many layers of management will fragment service delivery, impair communication, obstruct performance feedback loops, and foster information silo creation.
- **Functional Fragmentation:** Overspecialization is the enemy of organizational effectiveness. Unnecessary specialization fragments and impairs the management process.

Structural Factors Affecting Net Revenue

- **Corporate Structure:** Many U.S. hospitals are organized as Section 501(c)(3) charitable organizations under the Internal Revenue Code. Those that accept Medicare and Medicaid payments must comply with restrictive and resource-consuming conditions of participation. Hospitals are generally bound by state licensure requirements which vary from state to state. Finally, many voluntarily participate in programs offered by the JCAHO, CAP and other accrediting organizations. All of these factors add to service costs.

  Non-hospital organizations are able to offer services at far lower prices than traditional hospitals because they are generally sheltered from these costs. As the proliferation of non-hospital competitors demonstrates, it is not necessary to "be" a hospital to provide an impressive and growing menu of outpatient services. Although opportunities will vary from hospital to hospital, nothing prevents most hospitals from spinning off corporate entities unencumbered by the hospital's cost structure. A wide variety of carefully-selected existing and new outpatient services could be outsourced to those entities, potentially at lower and more competitive costs. Any potential corporate restructuring must be carefully evaluated to determine the net cost, accessibility, and quality benefit to the organization and to the community served.

As a result of *The Affordable Care Act*, related mandates and a resulting need to upgrade information systems, many hospital management teams have calendars that are impossibly full of "must do" initiatives. Many are operating with legacy structures that were established years ago and haven't been modified[1]. The potential for significant and very positive bottom line impact should move this subject to the top of the hospital's financial priority list.

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Editor's Note: Hospitals that subscribe or renew subscriptions to *IMPACT*, *IMPACT Plus* or the *IMPACT Operations Monitor* between now and May 30, 2015 may obtain a customized electronic organization chart of their hospital's current structure (see this example), at no cost upon request. If you would like to discuss your organizational structure needs, contact us at 816-587-2120 or by e-mail at info@bradyinc.com.

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