

Estimate of the Situation

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Paradigm Shift Options

It has been a recurring theme on these pages that we are in the early stages of a health care revolution. The changes already underway are systemic, profound and irreversible. We believe they will ultimately spell the end of the Third Party Payment System that has dominated hospital operations and medicine for more than half a century.

If we are correct, what does that imply for action on the part of hospital governing bodies and executives?

The Situation

The Third Party Payment System (not just the “Affordable Care Act”) has finally produced such absurd results that they can no longer be tolerated by the public at large.

- Forty percent of health care costs are directly attributable to the Third Party Payer System.
- Administrative costs and burdens imposed by the system have bankrupted thousands of individuals and businesses and now threaten the solvency of many states and the national government.
- The Third Party Payer System has already driven thousands of physicians from private practice, closed dozens of community hospitals with many more on the brink, and now threatens the economic viability of hundreds of small American towns.
- Approximately 5% of the population is responsible for half of total health care spending, while the 50% of the population with the lowest expenses accounts for only 2.7% of total spending.

We find ourselves in today’s precarious position precisely because every health care reimbursement scheme undertaken in the last half-century has insulated the consumer of health care services from paying (or even knowing) the real cost of the care provided. The primary goal of health planners has been to “socialize” or “spread” the costs of care over the entire population.

As a highly simplified example of how this works, consider what happens when three friends with very different appetites go out to dinner for the evening. The actual health care numbers are different (actually much worse), but the principle being illustrated still holds.

	<u>Diner</u>	<u>Meal Tab</u>
Sam		\$8.00
Marsha		\$35.00
David		<u>\$250.00</u>
	Total Tab	\$293.00

In a free market system, each diner pays for his or her own meal. However, if total meal costs are “socialized”, Sam, Marsha and David will each be required to pay \$97.67 (just divide the \$293.00 meal total among the three diners). This is a heck of a deal for David, not so much for Marsha and Sam. Today’s Third Party Payer System is designed to subsidize demand and hide costs. That is exactly what it is doing and it does it very well.

Action

As a practical matter, governing bodies and hospital executives would be well-advised to keep one foot in the legacy world and the other in the emerging market-based system. Accomplishing this will require considerable agility, keen attention to reimbursement and utilization changes, and vastly improved market intelligence.

We recommend:

- The exercise of extreme caution in capital spending or fixed asset acquisition that is dependent upon current utilization and reimbursement levels.
- Tracking the trajectory and velocity of service utilization changes, both inpatient and other.
 - Developing work force structure models, by job class, projecting current and projected FTE requirements by department and/or service.
- Identifying the most likely service-provision competitors, both hospital-based and non-traditional.
- Developing business models to project the financial consequences of moving selected services to entities, owned and otherwise, operating outside of the hospital’s corporate structure.
 - This includes developing alternate competitive charge structures.

Watch these pages for future service and event announcements on this topic.

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