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Understanding The True Cost of Care

By Gary Anthony & Jeff Jones

To manage value, healthcare providers must understand the true cost of care

Healthcare is one of the few industries that has escaped the need to address true cost and quality issues – until now. But understanding the true cost of care – not just revenues and expenses, but what it actually costs to deliver services across the continuum of care – is the critical first step to understanding how a provider can manage risk to succeed in the emerging value-focused environment.

Today, there are multiple factors pushing for lower healthcare costs – government actions, market-driven forces, and the choices of patients themselves. The growth of high-deductible health plans (HDHPs) and increasing patient responsibility have created a new reality around the cost of healthcare. Examples of hospitals charging \$25 for an aspirin and \$100 for newborn baby diapers fuel media attention and highlight the lack of true-cost data, as well as ineffective reimbursement models.

These forces are the impetus for new payment systems like

bundled payments, risk sharing, and other forms of value-based payment, as well as changes in managing utilizations. In 2016, CMS has introduced bundled payment programs that cover joint-replacement procedures, heart attacks and stents, and hip fractures. Successful execution under value-based payment systems requires that appropriate care is delivered with limited variation from patient to patient at the highest quality and lowest cost.

With this reality as the backdrop, how can healthcare providers tackle the elephant in the room – true costs? Nearly three years ago, Michael Porter and Thomas H. Lee summarized the issues as follows:

“There is ... a near complete absence of data on the true costs of care for a patient with a particular condition over the full care cycle, crippling efforts to improve value. The lack of cost information starts with widespread confusion about the difference between costs and charges. Most clinicians also have no way of knowing what things

actually cost or how much time care processes take. Without the ability to understand the costs of the care for specific conditions, or how costs compare to outcomes, efforts at cost reduction revert to power struggles and arbitrary cuts.^{1”}

Fortunately, a lot of progress has been made since Porter and Lee identified the dysfunction providers need to address. In Huron’s work with clients, through the use of data, reporting and business modeling, it is possible to illuminate the cost of services being delivered. This is as true for services in an ICU setting for critically ill patients, as it is for primary care delivered in a physician’s office.

Understanding the true cost of delivering care requires using highly-reliable and functional toolsets and ultra-efficient processes to transform raw data into actionable information to make more meaningful and sustainable changes. This type of analysis informs a breadth of decisions that providers can make for opportunities to improve

quality, reduce cost and increase value. For example the analysis:

- Yields solutions for bringing health professionals together in new and different ways to deliver care.
- Opens visibility into who are the high-value providers, sites of care, and service lines.
- Enables rationalization across multiple sites and true integration of services and providers following a merger or acquisition.
- Highlights reductions and unnecessary duplication of high-cost capital expenditures and equipment purchases.
- Affects decisions on how to provide care through new care delivery models or business models (e.g., a joint venture), or whether that type of care will be profitable.
- Helps a healthcare system make strategic decisions around eliminating or launching services to improve a provider's cost and quality position.
- Informs even more granular decisions around which surgical supplies are used, or determines better ways to manage high-cost drug utilization.

The resulting data can also inform decisions about targeted investments that can have a major impact on improving quality and lowering costs—thereby increasing

value. By conducting a deep analysis of true cost of care, it is possible to unlock visibility into a vast set of decisions that not only can be made, but frankly, must be made if a provider is going to achieve success in terms of raising quality and lowering costs.

By bringing together technology and expertise, it is possible to build and understand a true cost model that encompasses episodes of care across the continuum – from physician through rehabilitation. Using this model, value is defined as the quality of the care plus the patient experience, divided by the true cost.

Deep cost analyses and modeling across the continuum of care makes several benefits become apparent:

- **It is possible to prove that higher-quality care does, in fact, cost less.** Providers that are delivering the highest-quality care with the lowest amount of variation have the lowest true cost of care. By taking a closer look at the variations, it is possible to determine where the cost outliers are located and create consistency of care across the organization so that there are higher-quality outcomes and more predictable costs.
- **Providers will be empowered to enter into negotiations with payers.** With a full understanding of the cost of care, a provider can enter into both fee-for-service or value-

based care arrangements with an empirical service delivery model based on their market and patient population in a more informed manner. Ultimately providers can work with payers more transparently, based on as much or more information than the claims data the payers have.

- **Cost data illuminates revenue cycle issues, including right-coding, to maximize reimbursements under existing contracts.**
- **Further, the analyses help the provider to understand disease states in its populations so that the provider can build appropriate programs and supports.** Once the complexities are understood, it is possible to make better care decisions.
- **Ultimately, transparent information about costs empowers healthcare consumers to make informed decisions about their care and their options.**

Fundamentally, it is not possible to manage risk without having a deep understanding of cost. This poses a dilemma for many healthcare providers because the one certainty they face is that risk-based models will increasingly be the norm.

For the foreseeable future, healthcare providers will be living in a dual reimbursement world. Fee-for-service revenue will be under increasing margin

pressure. A growing percentage of fully capitated, value-based reimbursement will require rigorous attention to total cost of care and realignment of capital and human resources. The industry will reach a transformational tipping point, where organizations will begin to see that revenue cycle actually becomes much simpler in a more capitated environment, and managing value is where that focus must be. That value is a function of quality and true cost.

The management of performance against cost and value measurements is the discipline that will empower healthcare organizations. Healthcare leaders should focus on engaging their entire workforce and their physicians to understand this and embrace this new reality.

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Gary has more than 30 years of experience in healthcare and health information technology. He has led a wide range of engagements in the healthcare sector with a focus on clinical, business, and organizational transformation supported by the effective application of technology.

Recognized for the ability to create practical and effective solutions to complex business challenges, Gary has worked with payers, accountable care organizations, national health care organizations, large integrated delivery networks, academic medical centers, community hospitals, specialty hospitals, and pediatric hospitals to improve business effectiveness and the cost, quality, safety, and efficiencies of patient care through the transformational use of technology. He can be reached at gaaanthony@huronconsultinggroup.com.

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¹Michael E. Porter and Thomas H. Lee, Why Health Care Is Stuck — And How to Fix It, September 17, 2013, <https://hbr.org/2013/09/why-health-care-is-stuck-and-how-to-fix-it>

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