Modern Healthcare

Hospitals need to manage costs to compete effectively

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The business of healthcare is becoming increasingly muddled as **hospitals** and **insurance companies** engage in a competition of sorts. Each side is grappling to buy up physician practices to gain control over a bigger share of the premium dollar while managing costs, getting a holistic view of the continuum of care and securing a steadier flow of patients.

At first glance, the benefits might appear to be similar, but taking a closer look, the rationale for these acquisitions is slightly different. Hospitals have a lot to gain but need to take heed of specific obstacles.

Insurers are primarily seeking patient-care data and a deeper understanding of what it truly costs to take care of each patient on an annual basis. A prime example is **Indianapolis-based insurance provider WellPoint**, which absorbed CareMore Health Group in Cerritos, Calif., an operator that runs approximately 26 care clinics.

On the other side, as hospitals acquire physician groups and launch in-house insurance companies, they hope to cement their relationship with patients. They continue to pursue fee-for-service, volume-related revenue, while evolving their business models to assume risk and manage population health.

By associating their brands with reputable physician groups and expanding through acquisitions, hospitals are hedging their bets and investing in growth. No matter your view on the speed of market reforms from volume to value under either scenario, physicians are the key drivers of change. This is often a wise move that can generate significant value for all parties involved.

According to a 2013 study by Professional Research Consultants, over the past 25 years, an average of 80% of healthcare consumers have consistently laid claim to a hospital they would call “their own,” regardless of whether they had limited or abundant choices. Unlike insurers, many hospitals have a loyal following of patients, many of whom will provide referrals. There is a strong opportunity for hospitals to engage in marketing efforts and build their brands.

Hospitals continue to pursue a path toward more physician employment, with University Hospital in Augusta, Ga., announcing the allocation of $15 million toward practice acquisitions. North Shore-Long Island Jewish Health System's 2013 agreement with EmblemHealth, which involves three large medical groups (Manhattan's Physician

Group, Queens-Long Island Medical Group and Staten Island Physician Practice), has led to the development of one of the largest physician practices in the New York metro area. These groups are now part of AdvantageCare Physicians, which houses more than 400 primary-care physicians and specialists in 39 locations.

To sum it up, the teams in this competition have different playbooks and the benefits, as well as pitfalls, are slightly different for each.

A critical concern for hospitals is managing steadily evolving care. When moving from the traditional fee-for-service model to a capitation model, hospitals are taking on significantly more risk. As opposed to receiving payment for each service rendered and test administered, hospital management and board members need to have a line of sight to the cost of care for each physician's patient at a set fee, which generates a critical need to be more efficient than ever before.

Even with the increased risk and potential downside—if they are unable to meet patients' needs at set costs—hospitals are in an excellent position to engage in physician-group acquisitions and this trend will continue to accelerate, especially as the implementation of the Patient Protection and Affordable Care Act changes the healthcare landscape. But if hospitals want to be in the physician management and insurance business, there are potential pitfalls. More doctors under employment means the organization has to operate more cost-effectively in a capitated environment.

The challenge for hospitals is to have clear strategic objectives for their physician acquisitions. Often these acquisitions are reactive and are not part of a well-thought-out network plan.

Another concern is culture. A top-down management approach can undermine the accretive value of a medical group acquisition unless there is an appreciation of the culture of medical group practice management.

There is a tremendous opportunity for hospital systems to make great strides, as long as transactions are executed in a strategic manner and a solid governance structure is in place. Working with experienced M&A advisers who have knowledge and expertise in the market is also a critical component.

There is no single one-size-fits-all formula for success, but incorporating these guidelines into a well-designed approach will be key to achieving desired results.

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