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## Overview

- How to Move Beyond Compromise
- Danger of a Myopic Market View and a Reality Check on Industry Dynamics
- Internal Business Analysis
- Changing Market Dynamics

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## Negotiation Nirvana

- There are three basic ways of dealing with difference:
  - Domination: Only one side gets what it wants
  - Compromise: Neither side gets what it wants
  - Integration: Create a way for both sides to achieve what they (really) want
    - Mary Parker Follett, advisor to Theodore Roosevelt

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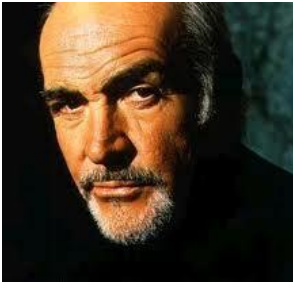
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## Domination Strategy May Be Flawed

- Perceived leverage that “dominates” the negotiation may yield missed opportunities
  - Did the dominant entity fully analyze the negotiation?
  - Is market power sustainable?

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## A Lesson From Sean Connery



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## Poor Negotiation Example #1

- **Know Your Market**
  - Sean Connery rejected “The Lord of the Rings”
  - Producers wanted “big name,” offer 15% of gross
  - He felt the movie was too complex
  - Each movie in the trilogy is ranked in the top 25 all-time highest grossing movies ever made
  - His salary would have been \$400 million for 1 movie, well over \$1 billion in total
    - Probably more with him in it

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## An Example Closer to Home



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## Poor Negotiation #2

- **Leverage May Be Fleeting**
  - Hospitals in Northern CA cost 56% more than in Southern CA per day
  - In Southern CA, half of the region's 167 hospitals are run by independents
  - Northern CA economics changed over past 10 years due to consolidation and closures
    - MCOs previously had a dominant position
    - 1 hospital system now represents 20% of the market

• LA Times "Hospital stays cost more in Northern California than Southern California", 3/6/11

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## The Inputs You Need For Integration

- Understand the Current and Future Market Dynamics (External Data)
- Analyze Your Existing Situation (Internal Data)
- Identify the Goals of Each Organization (Internal Data, External Data, and Communication)

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## Understanding Market Dynamics

- **Forecasting trends can open the door to opportunities**
  - MCOs often have greater insight to broader trends thanks to a data warehouse of ALL claims and geographic scope
  - Beware of a myopic view of your market

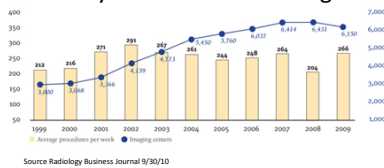
“Other Hospitals are our competition”

Are they really?

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## Imaging Competition – Reality Check

- **Diagnostic Imaging Centers**
  - 10 year growth rate in weekly procedures = 157%
  - Where is your business trending?



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## Surgery Competition – Reality Check

- **ASC growth in the US**
  - 4,106 in 2004 to 5,291 in 2010 (96% are for profit)
  - ASC Volume Up, Hospital Volume Down

**TABLE 5-6** Volume of surgical services grew faster in ASCs than in HOPDs, 2004-2009

Measure	Average annual percent change, 2004-2009	
	ASCs	HOPDs
Number of services per FFS beneficiary	6.8%	0.1%
Number of beneficiaries served	3.6	-1.7
Services per beneficiary served	3.1	1.8

Note: ASC (ambulatory surgical center), HOPD (hospital outpatient department), FFS (fee-for-service). To ensure comparability across sectors, the services analyzed consist of the same set of ambulatory surgical services. This set reflects services that were payable by Medicare when provided in an ASC in 2004.

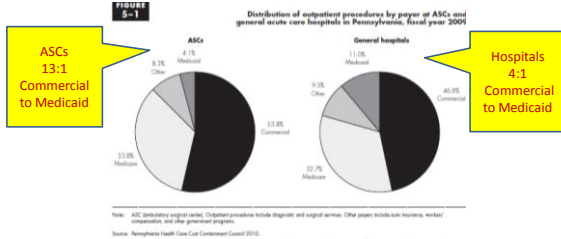
Source: MedPAC analysis of 5 percent center and outpatient standard analytic claims files, 2004 and 2009.

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## Surgery Competition – Reality Check

- Patient mix change may impact hospital OP surgical economics

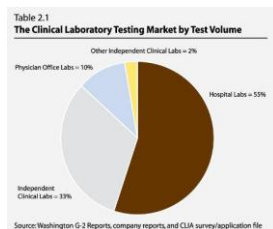
- PA study – ASCs have much greater Commercial mix



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## Lab Competition – Reality Check

- Hospitals still the major force
- But public lab companies seeing revenue growth of 10% annually



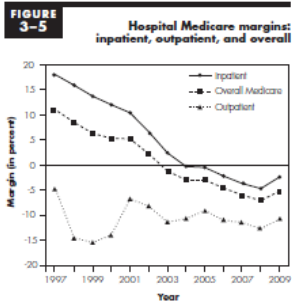
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## Internal Business Analysis

- Payer Mix
- Historic Trending of Volumes and Revenue
- Forecasting Future Business
- Cost and Margin Analysis

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## Medicare Margins Nationally



Source: MedPAC analysis of Medicare Cost Report file from CMS.

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- Slight Margin improvement in 2009 (but still negative)
- Future outlook
  - Payment to decrease 2.9%
  - Costs to increase 3% - 4%
  - Nonprofit, nonrural bear the largest burden

## Changing Payer Mix Implications

- What is the responsibility of Commercial payers to subsidize government payers, self pay and charity care?
  - What will that mix become under Reform?
  - Health Exchanges - Potential Cannibalization

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## Pitfall of the Classic Model

- Simply modeling prior utilization against proposed rates may not tell the full story
- Need a Crystal Ball (trend and sensitivity analysis)
  - What is happening in the payer's business?
    - Changes in Bundling Protocols
    - What product mix are they selling (HMO vs. PPO, etc.)
    - New Steerage via patient cost share or tiers

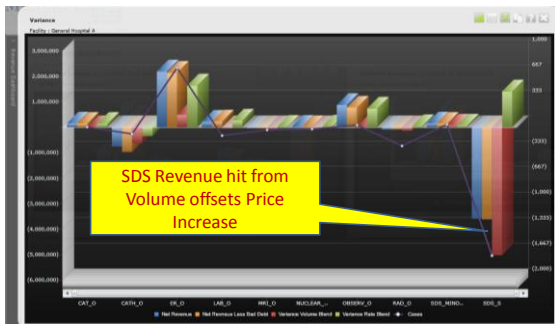
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## Revenue & Volume Comparison



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## Volume & Rate as Drivers



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## Integration Econ 101: $P \times Q$

- Healthcare as a traditional free market with transparency and plan design
- Can the Payer Direct Business: Tiered Plans
  - Aetna "Choose & Save"
  - United Health "Premium"
  - UPMC "Inside Advantage"
  - Highmark "Choice Blue"
  - Targeted Tiered Within Service Lines
- Pricing: Profit vs. Contribution Margin?

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## Your Choice PPO – A Tiered-Network Option Option 1 Summary of Benefits

TUFTS  Health Plan

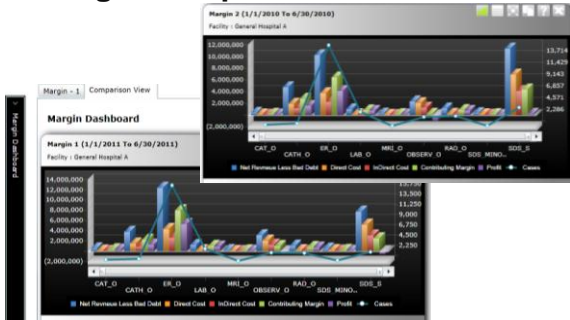
Outpatient Medical Care	In-network		Out-of-network (after deductible)
	Tier 1	Tier 2	
Non-routine Primary Care Physician Office Visits and Urgent Care	\$20 per visit	\$50 per visit	Plan covers 80%
Non-routine Specialist Office Visits and Urgent Care	\$35 per visit	\$70 per visit	Plan covers 80%
Outpatient Maternity Care (this office visit requirement will apply per visit up to 10 visits per pregnancy. After 10 visits, these services are covered in full for the remainder of your pregnancy.)	\$20 per visit	\$50 per visit	Plan covers 80%
Routine Eye Exams (one visit every 24 months)—You must use an EyeMed Vision Care provider to be covered at the in-network tier of benefits	\$20 per visit		
Allergy Injections	\$5 per visit		
Nutritional Counseling (when medically necessary)	\$35 per visit		
Speech Therapy (when medically necessary)	\$35 per visit		
Short-Term Physical and Occupational Therapy (up to 30 visits for each type of service per plan year)	\$35 per visit		
Spinal Manipulation (up to 12 visits per plan year)	\$35 per visit		
Colonoscopy Generally Associated with Symptoms (Including Family History of Cancer)—without surgical intervention	Covered in full		
Colonoscopy Generally Associated with Symptoms (Including Family History of Cancer)—with surgical intervention: at a freestanding outpatient surgery center	\$250 per admission		Plan covers 80%
Colonoscopy Generally Associated with Symptoms (Including Family History of Cancer)—with surgical intervention: at a hospital surgery center	\$250 per admission	\$1,250 per admission	Plan covers 80%

Tier 1 Hospital =  
Freestanding

How much Volume  
will Tier 2 Hospitals  
receive?

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## Margin Comparison



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## Margin Variance



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## Integration Econ 101: S & D

- **OON Specialists**
  - Supply and Demand out of synch
  - Yields high price but opens door for opportunity
  - Free market collaboration can reduce need for regulation
- **Hospital and MCO integration strategy on pricing and recruitment can yield improvement for patient, MCO, and Hospital**

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## Integration Keys

- **Determine your true external market, may need a broader view today**
- **Perform a proper internal business analysis**
- **Understand both sides core goals – they are not always in competition**
- **Be willing to be creative**

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## Contact Information

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