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The Revenue Equation

From deep inside the office, Wes listened to the gas turbine engines winding up on the Bell 230; the helicopter pad was a short distance from the east entrance of St. Matthew's Hospital. As heat from the compression ignited a mixture of fuel and air in the twin combustion chambers, the sleeping engines angrily awoke, shaking the building until the floors vibrated and the windows rattled.

Across the room, close up against the window, Pete Lister, the director of marketing, watched the Life Flight helicopter take off. Facing east, it hovered six feet above the ground while the pilot visually scanned his instruments. Then, smooth as a lazy Susan, the aircraft rotated 180 degrees west and lifted off into the icy morning sky.

"It's a marketing tool, you know," commented the director, turning from the window. He retrieved a pipe from the windowsill and fished for a tobacco pouch in the side pocket of his tweed sport coat. "With two helicopters and three fixed-wing aircraft, one of which is a Cessna Jet, we drop from the sky capturing patients from all over the state—patients that might otherwise be transferred from rural areas to Timpanogos Regional Medical Center or to Ensign Peak Regional Medical Center."

Lister opened the pouch, gently filled the pipe, and then tapped the tobacco down with his thumb. "We think our care's better, of course, and the flights are medically necessary. But they are marketing tools, still the same," he said, placing the pipe in the corner of his mouth.

As a tertiary care center, St. Matthew's Hospital was not a competitor with Peter Brannan Hospital, and the marketing director had been gracious enough to spend an hour with Wes who needed to know about marketing. Wes guessed Lister's age at forty-five. A closely cropped salt-and-pepper beard framed his square jaw. With his pipe and tweed coat, he looked more like a philosophy professor than the successful marketing director of a $200 million organization.

Lister lit his pipe. "It hasn't been long, you see, that hospitals have had to market their services. In the old days, under cost reimbursement, our physicians were able to create demand. Prospective payment systems put an

end to that. Although I haven't studied your statistics, there are probably several reasons for the decline in patient days your hospital's experiencing.

"In Utah, DRG reimbursement reduced the average length of stay in hospitals from seven to three days. In addition, many rural and suburban hospitals experienced out-migration as patients sought hospital care in larger cities."

"Why?" Wes asked.

"Transportation systems made it easier for patients to travel greater distances to receive hospital care. Also, there's the *'bigger is better'* syndrome." Lister returned to his desk. "The third reason is that many large hospitals have become more aggressive in marketing to rural areas. Since prospective payment systems have capped prices and reduced patient days, the only way to increase volume is by capturing patients from other facilities."

Wes was puzzled. "How do Salt Lake hospitals market to patients in Park City?" he asked.

"One way is by selling managed care programs to employers in your community that mandate the use of Salt Lake hospitals," Lister replied. "If your facility had lost the Mountainlands contract, a significant number of patients would have been channeled by employers to other inpatient facilities."

Lister's comments were consistent with Wes's observations. On his drive that morning to Salt Lake City, he had observed several highway signs advertising HMOs sponsored by metropolitan hospitals. Most were directed to employers. Although HMOs made sense from the standpoint of cost control, it hadn't previously occurred to Wes that they were also an effective marketing tool.

"Then what's the solution to our declining inpatient volume?" he asked.

"There are several possible solutions," Lister said. He retrieved a marketing report from his desk drawer. "The first is to recognize that in the current environment, hospital patient days represent a smaller and smaller portion of total healthcare cost. Notice the decline we've had in inpatient revenue as a percent of total revenue," he said, passing the report to Wes. "If Peter Brannan Hospital is to survive, it must supplement its inpatient revenue with other services."

Wes took notes attentively. "What types of services?"

"Outpatient services like laboratory and outpatient surgery, occupational medicine products and services for employers, durable medical equipment, rental agencies, etc.

"A second approach is to educate local employers about the negative impact of purchasing employee health benefit programs that send patients out of town has on the local economy. As patients leave the community, so do their dollars. Studies show that for every dollar that leaves the community for hospital services, an additional sixty cents is lost in retail revenue.

"The third approach is to increase inpatient volume by capturing a larger share of the local market. To do that, you might consider starting a hospital-

sponsored HMO. There are also a number of small rural hospitals in northern Utah and southern Idaho that can't offer the breadth of services Peter Brannan Hospital offers," Lister continued. "I suggest that you make a greater effort to capture their referrals."

Wes weighed what Lister was telling him. It made sense. "We need to pay more attention to marketing," he said. "Thanks for the insights."

To learn more about hospital pricing under prospective payment systems, read Supplement 4, *"Pricing Products and Services,"* which is found in Appendix One. For a detailed discussion on the design of hospital cost accounting systems, see the following supplements also in Appendix One.

Supplement 5—Information Needs of Managers
Supplement 6—Cost Accounting Taxonomies
Supplement 7—Designing Accounting Reports to Match Information Needs
Supplement 8—Designing the Pricing Module
Supplement 9—Regressing RVUs to Determine Fixed and Variable Costs
Supplement 10—Direct Materials and Hospital Overhead
Supplement 11—Ratio of Cost to Charges (RCC)
Supplement 12—The Use of Case-mix in Assessing Efficiency
Supplement 13—Rolling-up Standard Procedure Costs to Determine Product Costs

If you are not interested in this level of detail, continue by reading the next chapter.