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# Health Enterprise Partners

## *Seizing Opportunity in the Wake of Reform*

Executive Perspectives

*By Ezra Mehlman*

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## Background

It is no longer taken as a sign of sophistication to say that the Affordable Care Act (ACA) is “undefineable.” With Obama’s re-election on November 6<sup>th</sup>, certain ambiguities have crystalized into near-certainties. While considerable doubt persists regarding the pace and form of health reform’s implementation, a second Obama term assures us that the central tenets of the ACA will not be eliminated. Yet, against this backdrop of reform, it remains unclear how institutions will react to the complex system of carrots and sticks that has been erected around them. It is the purpose of this study to identify what types of bets high-performing hospital systems, health plans, and health care IT companies are making in the wake of reform. Equipped with these findings, we might approach an understanding of what the future holds—and how we might pre-empt legislative mandates in shaping it.

## Research Methodology

### Survey

The cornerstone of our research was a survey that we distributed to our network of approximately 500 hospital systems and integrated delivery network (IDN) administrators, health plan executives, and health care companies. The survey, which is reproduced in its entirety in the final section of our report, probed several of the most widely discussed implications of reform. In designing the study, we were largely focused on pressure-testing the

conventional wisdom, and examining the extent to which respondents agreed with several of reform’s underlying hypotheses around the five key topics shown here.

### Interview

To complement the survey, we had the opportunity to conduct an in-depth interview with John McWhorter III, SVP of Baylor Health Care System and President of Baylor

### *Survey Focus Areas*



University Medical Center Dallas. Our interview with Mr. McWhorter provides specific, executive-level insight into how one of the most successful hospital systems in the country is taking advantage of the opportunity of reform. This interview appears in the corresponding section of this report.

### **Executive Discussion**

Our research findings were presented in a teleconference bearing the same title of this study on November 19<sup>th</sup>, 2012. This teleconference featured an executive discussion featuring HEP, Kaveh Safavi, Managing Director and Health Industry Lead of Accenture, and Scott Whyte, VP of Information Connectivity and Dignity Health. The insights provided by these two executives closely informed our research effort.

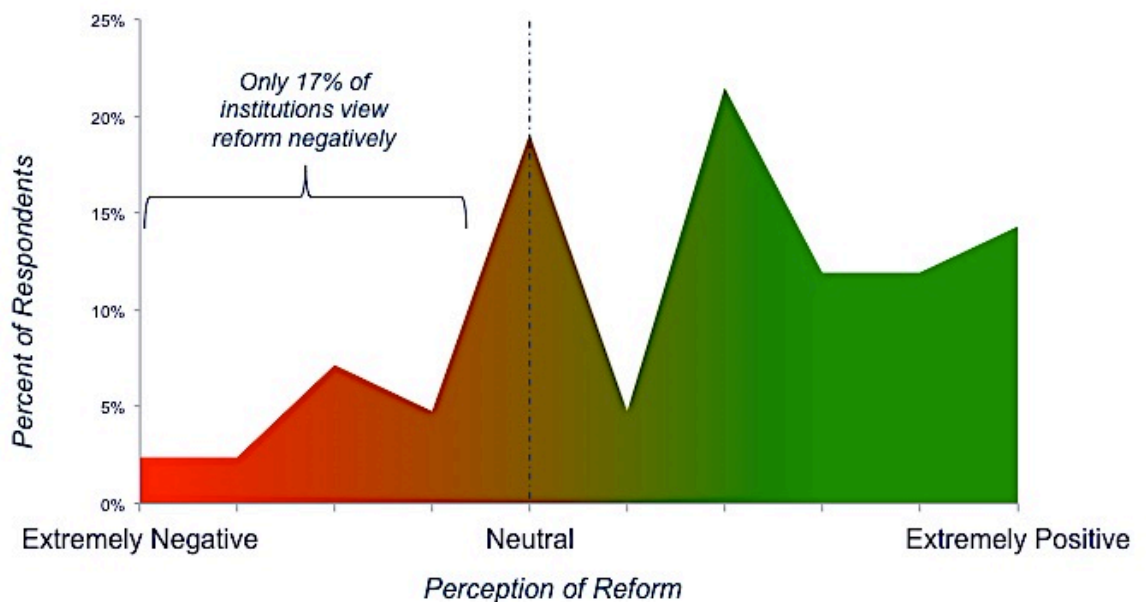
## **10 Key Findings**

The following recommendations were distilled from our survey research, and completed by interviews with health system and health plan administrators:<sup>1</sup>

**#1—Health reform is viewed favorably by most.** Beginning our examination with the philosophical question, “*Is reform good?*,” we found that the overwhelming majority of respondents regard

reform as having a positive impact on their organizations, with only 17% viewing reform negatively (as depicted in *Exhibit 1*). It is perhaps unsurprising that the most progressive institutions—which

***Exhibit 1: How Do You View Health Reform?***



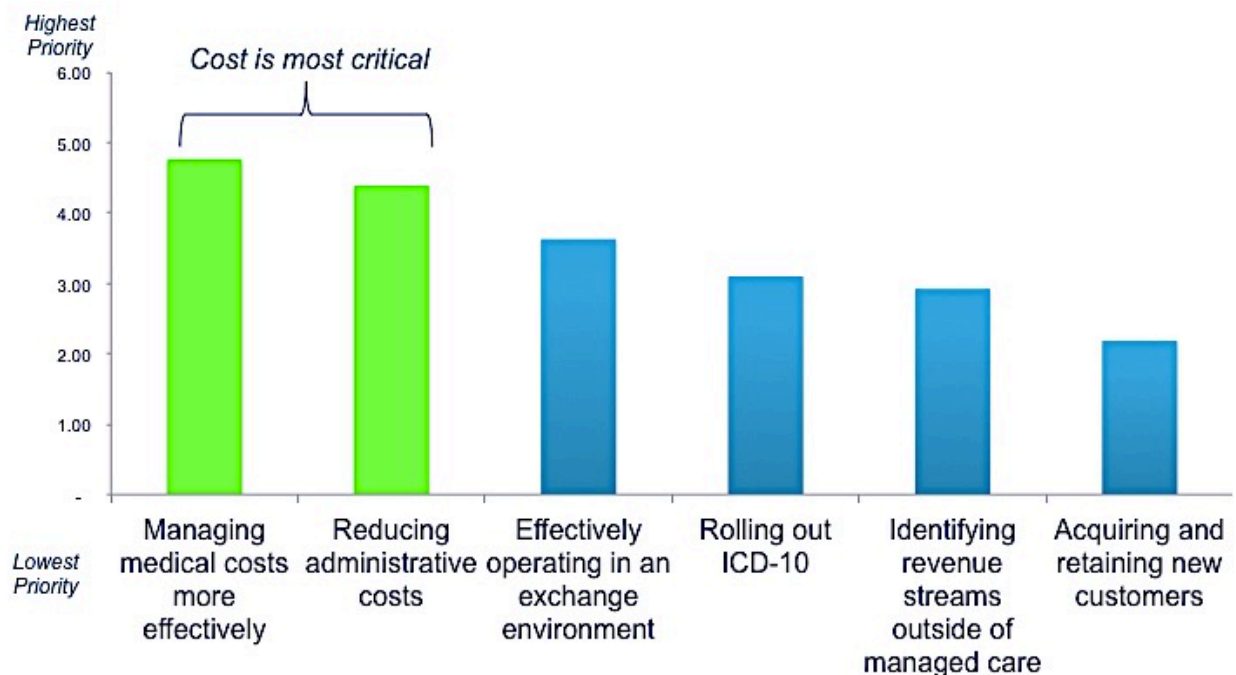
<sup>1</sup> A methodological note: In the course of conducting our primary survey research, we posed some questions that had been posed separately in other contexts. These include the following: Boston Consulting Group. *How Health Reform Will Change the Insurance Landscape*, 2012. ReviveHealth. *Turning the Corner Towards 2014: National Payer Survey*. August 2012. Deloitte Insights. “Health Care CEOs’ Perspectives on the Future.” *WSJonline*. July 25, 2012.

comprise the lion's share of our survey participants—view health reform as an opportunity to execute on a strategy that they have developed for some time.

This perspective is captured succinctly in the words of a Chief Financial Officer of a top 5-ranked IDN<sup>2</sup>, *"We are pursuing our strategy essentially without regard to who wins the election. We believe the future will require much more aligned incentives between payors, providers, and patients...so all have some appropriate 'skin in the game.' We are headed to taking accountability for the health of our community and driving our necessary utilization."*

**#2—Cost reduction remains the top payer priority.** Focusing our attention first on the payer market, we were interested in examining how the ACA is impacting the strategic priorities of health plans. Asking administrators to prioritize a variety of challenges related to health reform, we see that considerations related to decreasing the cost of care are regarded as the most acute pain point for respondents (as displayed in **Exhibit 2**).

**Exhibit 2: Payers: Please Prioritize the Following Challenges**



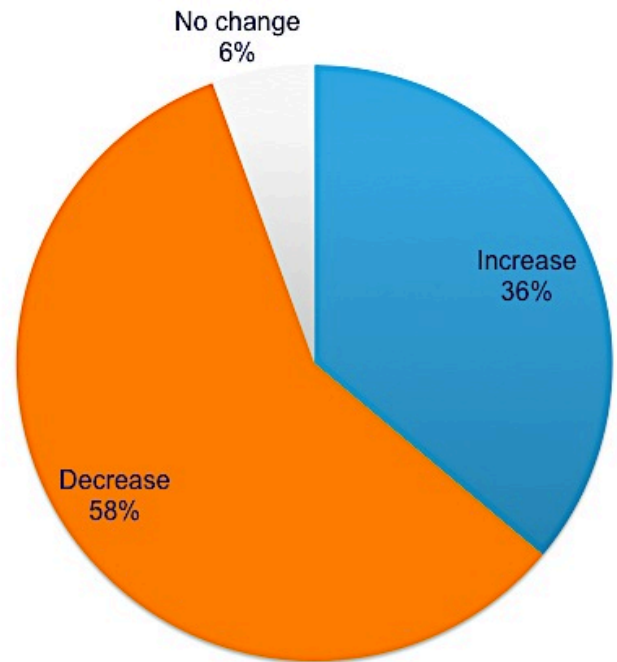
This is notable in that, for all the talk of diversification, of finding revenue streams outside of managed care, most payers are still focused on improving their central business of covering lives.

<sup>2</sup> As ranked by *Modern Healthcare*, January 23, 2012.

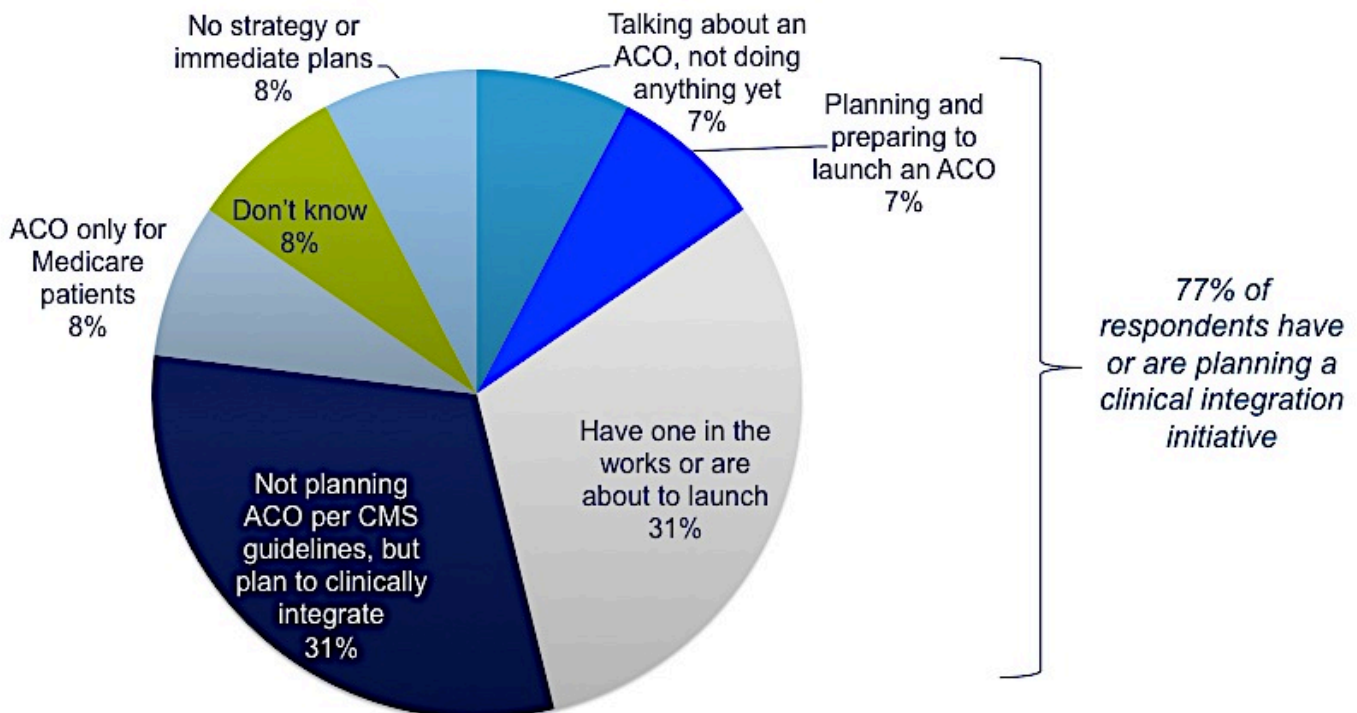
**#3—As private pay rates decrease, most health systems plan to clinically integrate.** As health systems seek to decrease their cost base, it is not surprising that most respondents in the industry are projecting a decrease in private pay rates, as depicted in *Exhibit 3a*.

In this world of payment ambiguity, we find that the majority of hospital systems and IDNs—77% —are executing or planning to undertake clinical integration initiatives with their physicians. The keyword here is narrow networks: by linking more closely with their affiliated physicians, health systems can more directly manage the cost of providing care effectively. *Exhibit 3b* provides a snapshot of the extent to which health system respondents are planning various forms of clinical integration.

**Exhibit 3a: Will Health Reform Increase or Decrease Hospital Private Pay Rates**



**Exhibit 3b: Health Systems: Which of the Following Are You Planning**

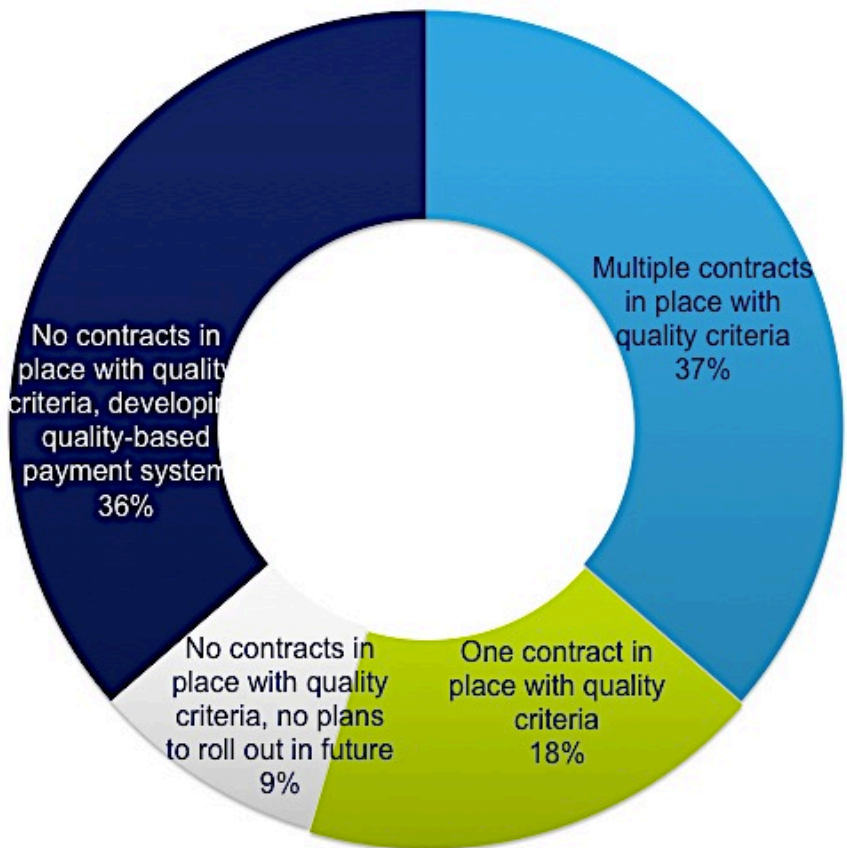




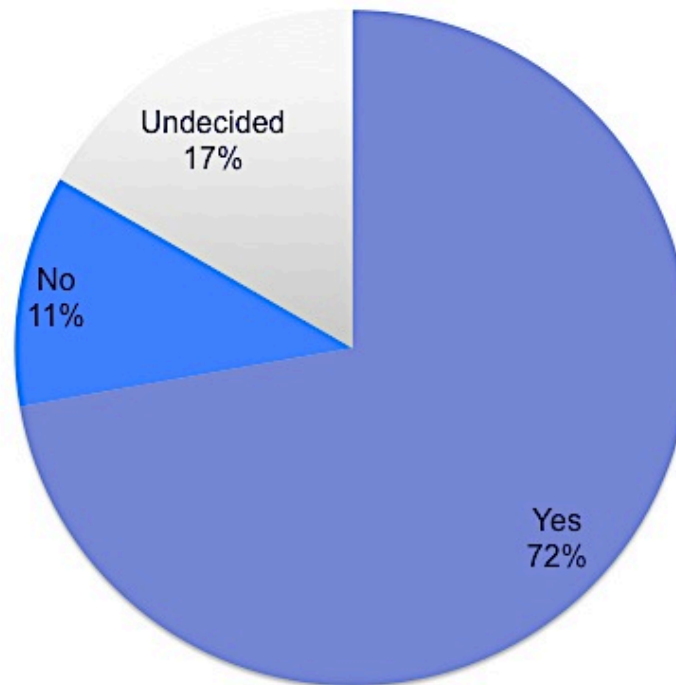
**#4— Most payers Have already developed pay-for-performance Initiatives.** As health systems brace for reform through physician alignment, we see payers moving boldly ahead of legislative mandates in rolling out pay-for-performance initiatives. Our research suggests that the majority of payers have already developed a P4P program, with another 36% having one in the works. **Exhibit 4** displays this trend.

***Exhibit 4: Payers: Describe the State of Your Quality-Based Reimbursement Program***

**#5— Exchange participation will be widespread.** It would be impossible to conduct a survey of payer priorities in the post-reform era without touching upon the topic of the exchanges. Perhaps unsurprisingly, we found that the overwhelming majority of payers plan to participate in the exchanges. Furthermore, the vast majority of industry participants believe that payers *should* participate in the exchanges. We see this trend reflected in **Exhibit 5** on the following page.



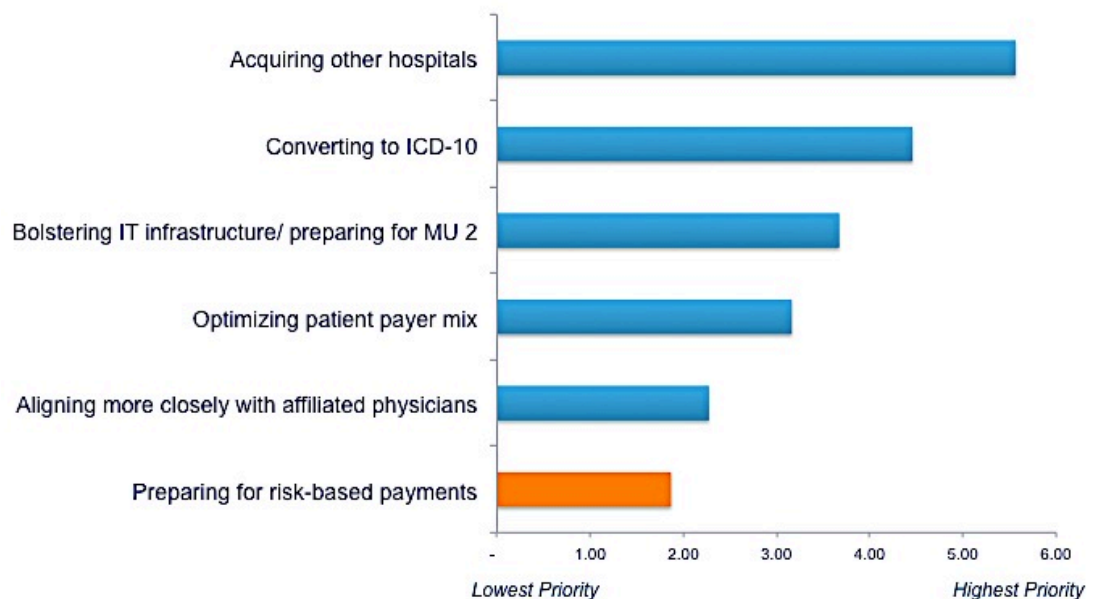
**Exhibit 5: Should Payers Participate in Exchanges?**



**#6: Providers remain under fee-for-service mindset.** Shifting our attention to the health system and IDN market, we were interested in identifying how prominently a variety of reform-related trends figured into the decision-making process of providers. Just as we

did for payers, we asked providers to rank-order a variety of pain points in terms of relevance to their organization. What is remarkable is that the lowest priority item—shown at the bottom of **Exhibit 6**—is preparing for risk-based payments, while most of the other priorities (such as optimizing patient

**Exhibit 6: Hospital Systems: Please Prioritize the Following Challenges**



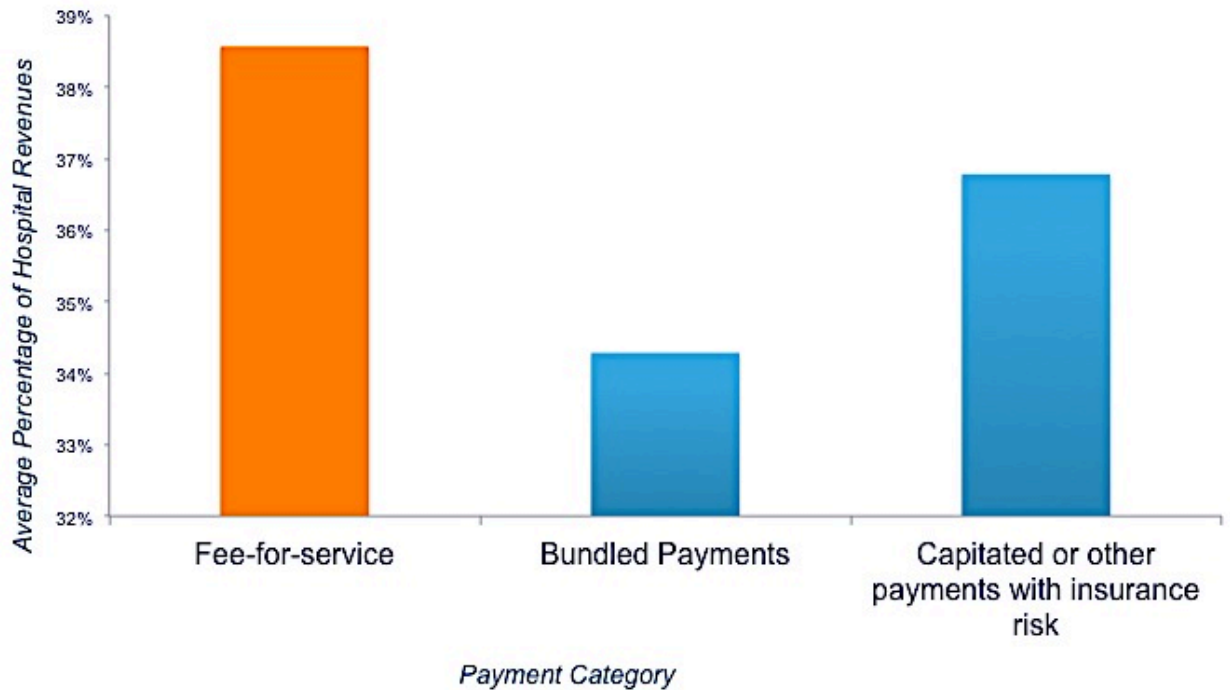


payer mix) adhere to a fee-for-service worldview.

**#7: Fee-for-service will continue to represent meaningful share of hospital revenues moving**

**forward.** Probing a bit deeper into this phenomenon, we asked respondents how the revenue mix of hospital systems and IDNs will be constituted five years from now between risk-based

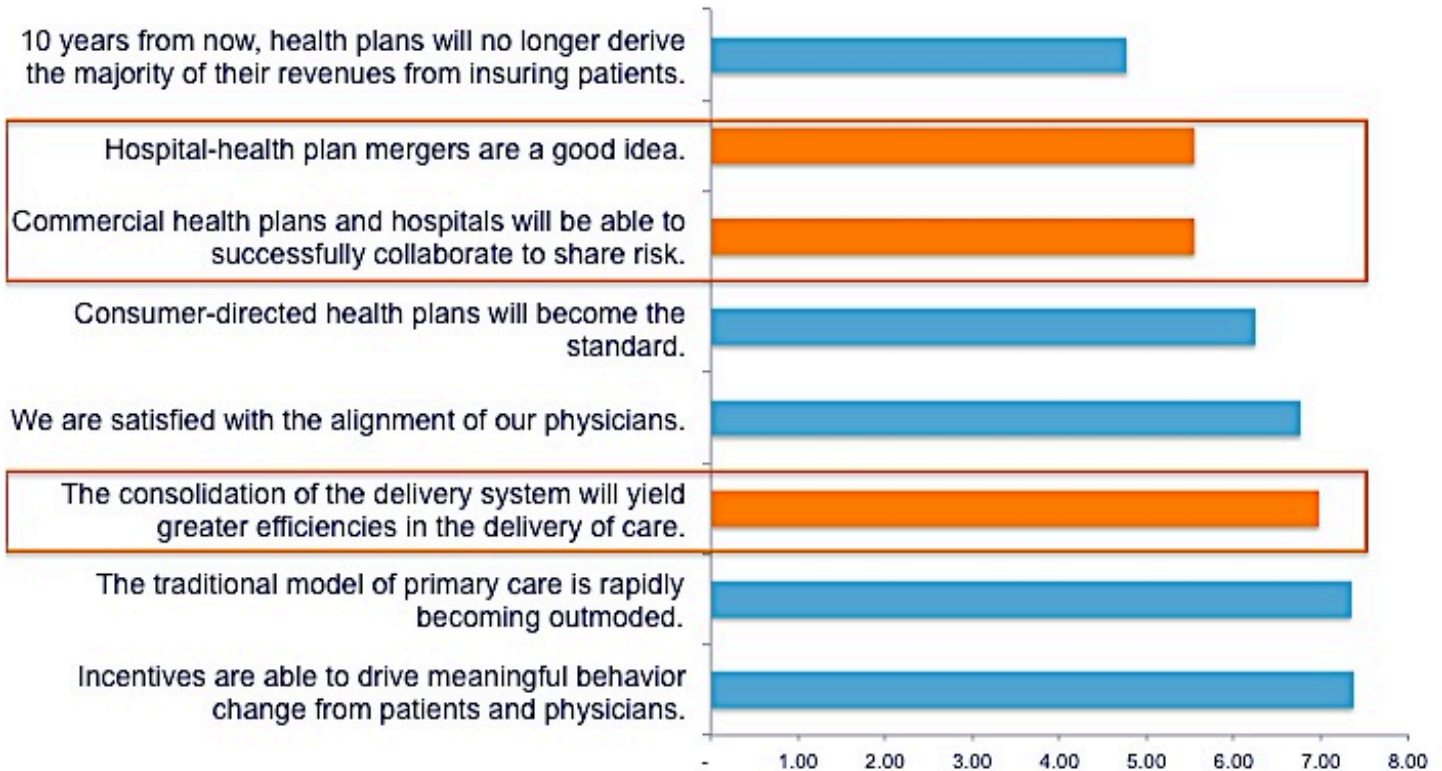
***Exhibit 7: In the next 5 years, the revenue mix of hospital systems will be divided according to the percentages below***



payments on the one-hand and fee-for-service payments on the other. Consistent with the previous finding we see that most believe that fee-for-service will continue to represent the most meaningful portion of hospital payments.

**#8—Consolidation welcomed with open arms.** While providers may be stuck in a fee-for-service worldview, one health reform trend has been welcomed wholeheartedly by health systems: consolidation. We laid out a variety of statements that have been used to characterize the restructuring of our health care delivery system. As evidenced by the responses in **Exhibit 8** on the following page, most respondents agreed with the philosophy of consolidation: such as that hospital M&A is a good idea, and that the centralization of resources will provide better care.

**Exhibit 8: To what extent do you agree or disagree with the following statements?**

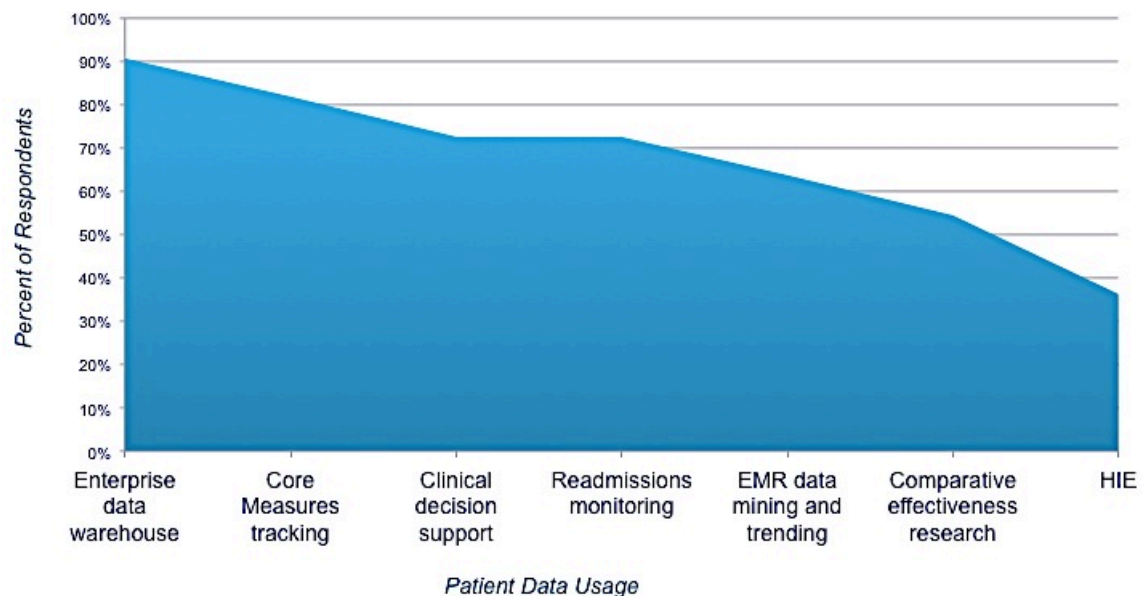


**#9— Enterprise data warehousing is the fundamental building block of big data initiatives.** As a fund largely focused on

healthcare IT, we were interested in gaining insight into how hospital systems are leveraging patient data in the context of health reform. To do so, we laid out a variety of innovative applications of data in hospital settings; by identifying

which applications of data were more common than others, we were able to effectively plot an adoption curve. This curve reveals that enterprise data warehousing (EDW) seems to be the common foundation

**Exhibit 9: Hospital Systems: In Which of the Following Ways Are You Using Patient Data?**



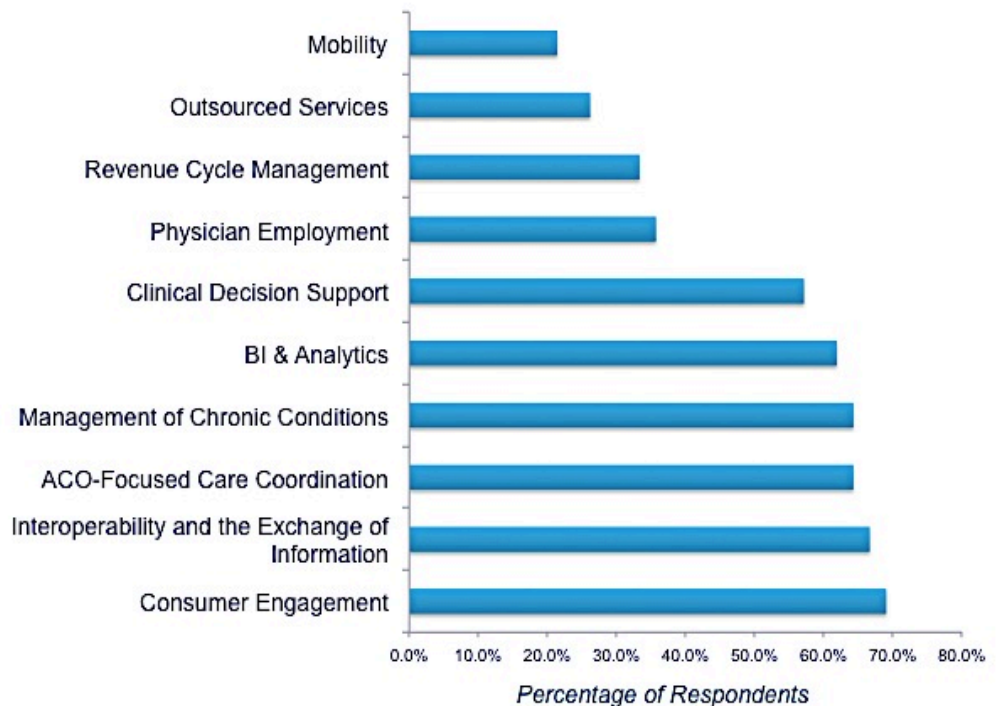
upon which most other IT initiatives are built. On the opposite end of the spectrum, we see that less than 50% of respondents are partaking in health information exchange (HIE). **Exhibit 9** features this adoption curve.

**#10— Consumer engagement is king, though most organizations lack sufficient social media**

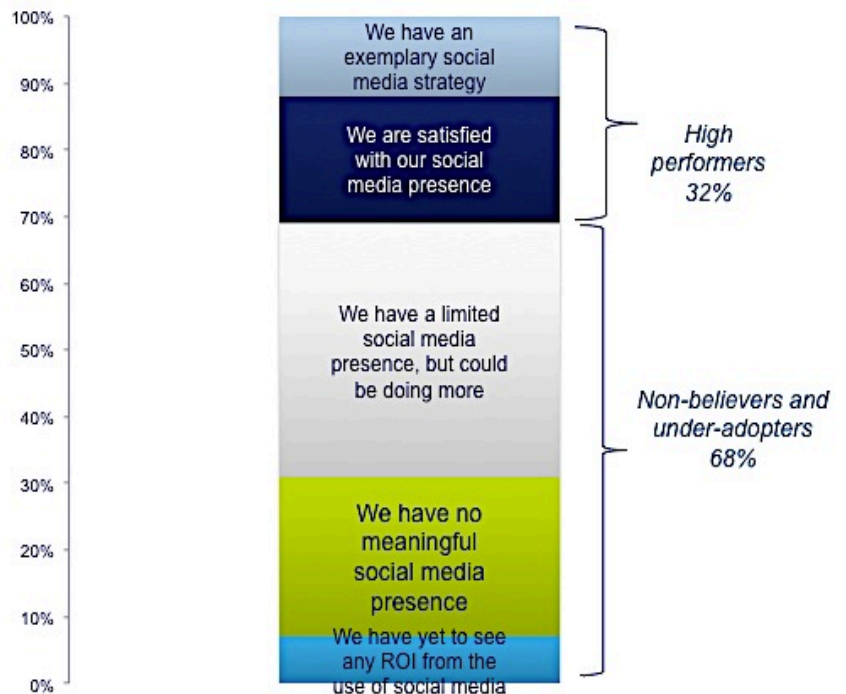
**presence.** The under-penetration of HIE is notable when viewed against the areas that health system administrators plan to target for investment in the next 12 months. As shown in **Exhibit 10a**, interoperability and the exchange of information is a sector that nearly 70% of respondents plan to invest in.

The other takeaway here is that consumer engagement is the highest investment priority across all respondents. What makes this focus on consumer engagement remarkable is that nearly 70% of institutions believe that they are getting no ROI from their social media efforts (**Exhibit 10b**), or that they could be doing more in this space. Consumer engagement could be viewed as both the #1 priority and the #1 pain point.

**Exhibit 10a: Which of the following do you plan to target for investment this year?**



**Exhibit 10b: How would you rate your social media strategy?**



## Conclusions

In reflecting on the research, four essential conclusions emerge. These are captured in the table below.

| 1 Consolidation is the first step   | 2 Fee-for-service is going nowhere fast   | 3 Consumer engagement eludes most...   | 4 Health plans are moving in advance of legislation   |
|---|---|--|---|
|    |    |    |    |
| <ul style="list-style-type: none"> <li>• Over 60% of hospital systems plan to clinically integrate with physicians</li> <li>• Overwhelming majority believe that consolidation will yield greater efficiency</li> </ul> | <ul style="list-style-type: none"> <li>• Respondents ranked "preparing for risk-based payments last among 6 priorities"</li> <li>• Most believe FFS will continue to be a meaningful part of revenues in 5 years</li> </ul> | <ul style="list-style-type: none"> <li>• Consumer engagement is the #1 priority for investment in the next year</li> <li>• Most believe that their organizations fall short in social media efforts</li> </ul> | <ul style="list-style-type: none"> <li>• Most have already rolled out quality-based reimbursement contracts</li> <li>• Most health care insurance companies plan to participate in an exchange</li> </ul> |



As mentioned earlier, we were fortunate to engage John McWhorter III, President of Baylor University Medical Center and SVP of Baylor Health System in a written interview regarding his organization's strategic priorities. His responses are reflected below.

**1. *What specific opportunities and challenges does reform create for your organization?***

**Opportunities**

*For Baylor Health Care System as other hospitals and health systems, reform should result in more people obtaining some form of government sponsored or government assisted payment for health care. The 18-26 year old population has benefited from insurance reform allowing students and young adults to remain on parents' insurance policies. Affordability for private insurance should go up as premiums drop.*

*The design of incentives across all groups (hospitals, physicians, consumers, and insurers) should improve. Incentives to provide value based care and eliminate waste should be enhanced. We will move from a "per click" to a bundled payment. For Baylor this means opportunities to provide direct contracting with employers, bundle payments with post acute care providers, and study the option of providing "carve'-outs" for chronic diseases.*

*Incentives surrounding implementation of electronic medical records for all stakeholders are also enhanced under health reform. Baylor is undertaking a massive (\$200 million plus) electronic conversion including physician offices, clinics, and hospitals that should be complete in 2013. Reform will also result in more accountability for the patient in the form of higher out of pocket costs and more responsibility for personal care; we will discuss Baylor employees and personal care in the next few questions.*

**Challenges**

*Some states will not implement a state exchange (Texas being one of those states) and we have yet to see what a federal exchange would look like. Additionally, there are 100,000 or more pages of regulations to be written all impacting delivery of care. We have many unknowns; who will collect*

*1040 information to determine level of income for employees to qualify for an exchange? How will penalties be collected?*

*States such as Texas that will not accept Medicaid expansion will really harm hospitals like Baylor. We will lose disproportionate share funds (millions) with no relief from the uninsured. Best-case scenario in Texas was that half of the uninsured would have access to a payment; without expansion of Medicaid that number will be less than 20 percent. Of 6 million uninsured Texans (27 percent of population) less than 1.5 million will be eligible for Medicaid.*

*We should also mention that ICD10 will eventually be implemented which will have a significant impact on rural providers and small hospitals.*

**2. *How is Baylor adapting to new payment models since a major thrust of the Affordable Care Act is to transfer payment risk to hospitals?***

*Baylor accepts the premise that legislators will try and transfer insurance risk to providers in the form of Accountable care. Baylor is addressing this in six areas: (a) using our employee group as an experimental insurance pool, (b) partnering with insurance companies to reduce unnecessary care in a shared savings model, (c) direct contracting with large employers in narrow networks, (d) developing an accountable care organization called Baylor Quality Alliance, (e) developing a robust post acute care network for bundling, and (f) exploring insurance options for the future.*

*Baylor Quality Alliance is our version of the ACO with nearly 2,000 physicians participating. The physicians will be working on standardization of care, reducing variation, adopting best practice, and sharing in cost savings models approved by the federal government. The BQA will provide care for all Baylor employees in the future which is a group of 34,000 insured lives. It is conceivable that Baylor along with other large health systems will partner together to reach 100,000 insured lives managed by an employee group.*

*Baylor already has direct contracts with two of the largest employers in the country in the Dallas Fort Worth area. These are narrow networks with substantial out of pocket costs for employees who receive care out of network. We also have an agreement with a large insurance company that shares savings on readmissions for several key conditions. The shared savings model is a 50/50 split of savings.*



*Baylor has developed a robust post acute care network including 4 inpatient rehabilitation hospitals, 38 outpatient clinics, one LTAC, and two inpatient hospice units. This will be useful for bundling of orthopedic procedures and other conditions in the future.*

**3. How is Baylor approaching the challenge of engaging consumers?**

*Baylor has become very active with our own employees to study ways in which incentives may modify behavior. We require all employees to complete health risk assessments and coaches are encouraged assigned for chronic conditions. We no longer hire smokers and have eliminated fats and sugar drinks from all environments. We require a flu vaccine and are now working on body mass index.*

*For consumers we offer navigators for service lines (oncology and neuroscience) to assist patients with good choices and we are reassessing the cost benefit of health screenings. The market is driving this to a great extent through high deductible plans and narrow networks. Employees are now in “steerage networks” designed to keep care in a network. Baylor must be a choice in these networks.*

**4. What are some key considerations that administrators should weigh in striving for alignment with physicians in the process of clinical integration activities.**

*The spectrum of incentives is one that is difficult to navigate but essential for our future. How much money is necessary in the form of appropriate economic incentives to change behavior? How much money is in the form of “carrots” or “sticks”. Sticks in the Dallas market are “withhold” provisions similar to the old HMO contracts. Withholds may be a dirty word in your market. Partners in Boston utilizes a withhold of 10 to 20 percent depending on the specialty or service.*

*To manage care data must be available, accurate, timely, and transparent. How well is your organization doing in those four areas?*

*What is the appetite among your physicians in sharing risk? Is that something they are open to, embrace, or shrink away from? The attitude toward risk based payment will determine to a great extent the acceleration of integration in your community.*

*The number of specialists in your community will to a great extent determine your integration. In a specialty with too many doctors and not enough patients, physicians may eager to share risk or be a part of your network. For those specialties that are scarce, attitudes may be different. We take the position that it is best to work with those specialists who are open to working with you first to get quick wins with the understanding that you will need all specialists eventually to offer a network.*

*We should not forget about hospitals based physician groups and their impact on the cost of care and the opportunity to reduce the cost of care and provide value.*

## Survey Questions

The following questions comprised our survey, which we conducted over 3 weeks in October.

**1. Please provide your Name, Title, Organization and Email Address.**

- First Name
- Last Name
- Title
- Organization
- Email Address

**2. My organization is best described as a:**

- Hospital System or Integrated Delivery Network
- Health Plan
- Physician Group
- Healthcare IT or Services Company
- Other (please specify)

**3. How would you rate health care reform's effect on the future performance of your organization?**

Extremely Negative (1)

Neutral (5)

Extremely Positive (10)

**4. To what extent do you agree or disagree with the following statements?**

- The traditional model of primary care is rapidly becoming outmoded.
- The consolidation of the delivery system will yield greater efficiencies in the delivery of care.
- Commercial health plans and hospitals will be able to successfully collaborate to share risk.
- 10 years from now, health plans will no longer derive the majority of their revenues from insuring patients.
- Incentives are able to drive meaningful behavior change from patients and physicians.
- Consumer-directed health plans will become the standard.
- Physician alignment is a major challenge.
- Hospital-health plan mergers are a good idea.

**5. Please prioritize the following challenges in terms of relevance to health plans. (1: Most Important, 6: Least Important)**

- Managing medical costs more effectively
- Reducing administrative costs
- Effectively operating in an exchange environment
- Rolling out ICD-10
- Identifying revenue streams outside of managed care
- Acquiring and retaining new customers

**6. Please prioritize the following challenges in terms of relevance to hospital systems and IDNs (1: Most Important, 6: Least Important)**

- Optimizing patient payer mix
- Aligning more closely with affiliated physicians
- Preparing for risk-based payments
- Bolstering IT Infrastructure/Preparing for MU 2
- Converting to ICD-10
- Acquiring other hospitals

**7. In your opinion, will health care reform increase or decrease hospital system and IDN private pay rates?**

- Increase
- Decrease
- No change

**8. Hospital Systems and IDNs Only - ACO Strategy: Which of the following best describes your current ACO strategy?**

- Talking about an ACO, not doing anything yet
- Planning and preparing to launch an ACO
- Have one in the works or are about to launch
- Not planning ACO per CMS guidelines, but plan to clinically integrate
- ACO only for Medicare patients
- Don't know
- No strategy or immediate plans

**9. Health Plans Only - Please describe the state of your quality-based reimbursement program.**

- Multiple contracts in place with quality criteria
- One contract in place with quality criteria
- No contracts in place with quality criteria, no plans to roll out in future
- No contracts in place with quality criteria, developing quality-based payment system

**10. Which of the following strategies should health plans undertake in the next 3-5 years? (Check all that apply)**

- Acquire physician practices
- Acquire Medicare Advantage plans
- Acquire HIT companies
- None of the above

**11. How do you see your workforce changing in the next 5 years?**

- Increased recruiting challenges
- Decreased recruiting challenges
- No change

**12. Which of the following areas, if any, should hospital systems, IDNs, and health plans target for investment in the next year? (Check all that apply)**

- ACO-Focused Care Coordination
- Consumer Engagement
- BI & Analytics
- Management of Chronic Conditions
- Outsourced Services
- Revenue Cycle Management
- Clinical Decision Support
- Interoperability and the Exchange of Information
- Physician Employment
- Mobility
- Other (please specify)

**13. How would you describe your organization's application of social media?**

- We have no meaningful social media presence
- We have a limited social media presence, but could be doing more
- We are satisfied with our social media presence
- We have an exemplary social media strategy
- We have yet to see any ROI from the use of social media
- Other (please specify)

**14. In the next five years, the revenue mix of hospitals systems and IDNs will be divided across the following categories according to the percentages below. (Specify percentage number in each category)**

- Fee-for-service (includes DRGs for services you provide)
- Bundled payments (includes services you don't directly provide)
- Capitated or other payments with insurance risk

**15. Hospital Systems and IDNs Only - In which ways are you currently using patient data? (Check all that apply)**

- Enterprise data warehouse
- Clinical decision support
- EMR data mining and trending
- Core Measures tracking
- HIE
- Comparative effectiveness research
- Readmissions monitoring
- Other (please specify)

***16. How should hospital systems and IDNs prioritize the following considerations in transitioning to ICD-10? (1:Most Important, 4: Least Important)***

- Resourcing the transition
- Training staff
- Maintaining two coding systems simultaneously
- Avoiding payment delays

***17. Should health plans participate in exchanges?***

- Yes
- No
- Undecided

## Acknowledgements

HEP would like to thank the following individuals, who were instrumental to our examination of the market:

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*Dignity Health*