

2010

# THE HEALTHCARE SUPPLY CHAIN SURVEY

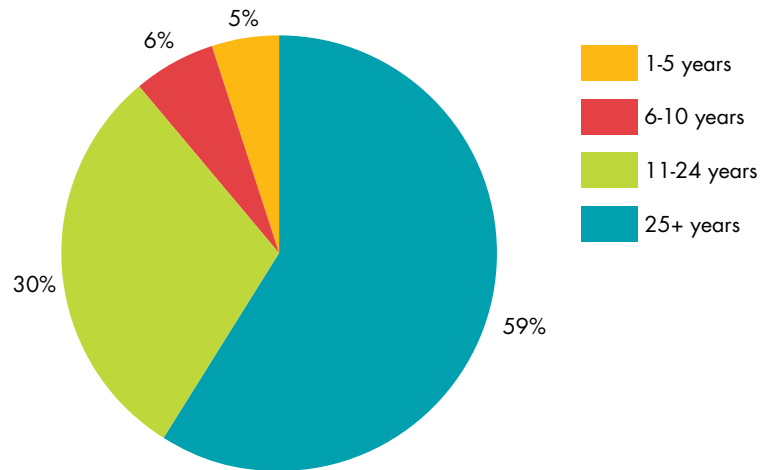


2010 IDN Summit Events & Supply  
Chain Survey Series Sponsored By:



At a time when healthcare reform, declining reimbursement from both public and private payers, and a prolonged economic downturn are putting healthcare providers under intense pressure to achieve new cost efficiencies, the healthcare supply chain is a source of both hope and concern. The hope is that through efficiencies such as new forms of consolidated buying, automation of the supply process and common data frameworks, savings can be found in areas such as medical-surgical supplies and contracted services. The concern is that constrained capital and labor spending will place stress on the departments that are able to deliver on those efficiencies.

Respondents' Healthcare Experience



This is an opportune time, then, to present the first independent snapshot of the healthcare supply chain.

IDN Summit and Expo last year mailed a survey to 728 healthcare executives of various aspects of supply chain management at integrated delivery networks and health systems across the United States, and 139 responded. While that may appear to be a small sample, these executives tend to be key leaders in supply chain management, with three quarters of them identifying themselves as chiefly responsible for their organizations' supply chain function. Some 48% of respondents represent systems with more than 1,000 beds and nearly three quarters represent organizations with more than 500 beds, placing the respondent organizations among the largest in the nation, with hundreds of millions of dollars in annual supply spending.

This is also an experienced group. Nearly nine out of 10 respondents had spent at least 11 years in healthcare, and 59% had at least 25 years' experience. Most respondents were either at the vice president or director level and are the people primarily responsible for the supply chain. A handful of respondents are chief executive officers, chief operating officers or administrators. Respondents represent a geographic cross-section of the country.

Most respondents (91%) describe themselves as fully involved in purchasing of medical-surgical supplies, clinical products (88%), capital equipment (75%), physician preference items (75%) and purchased services (61%). They are somewhat less involved in areas such as revenue cycle management, waste management and linens management.

The survey results provide a portrait of the industry in its current state and a baseline for which to conduct further research in order to begin analyzing the data over time.

*The IDN Summit Research Series is an on-going research project to provide a better understanding of the links in the healthcare supply chain. This research will provide key insights to foster an improved healthcare supply chain and identify key trends impacting the industry. To participate in future research please contact Lisa Ponssa at [lisa@idnsummit.com](mailto:lisa@idnsummit.com).*

## TOP ISSUES

As the chart below shows, the survey results reveal a range of factors that influence respondents' daily work lives. Controlling costs is obviously the most important factor; not a surprise in today's healthcare world.

Nearly three quarters of respondents were concerned about the potential effects of healthcare reform.

Although respondents ranked environmental issues relatively low, it may be because many organizations have already adopted many "green" initiatives, a subject we will return to later in this report.

Not reflected on the chart are a number of other responses that reflect the wide range of concerns affecting supply chain managers today. They include:

*"Potential unionization of health care employees caused by the labor shortage and labor productivity challenges—the current California nursing H1N1 complaints are an example."*

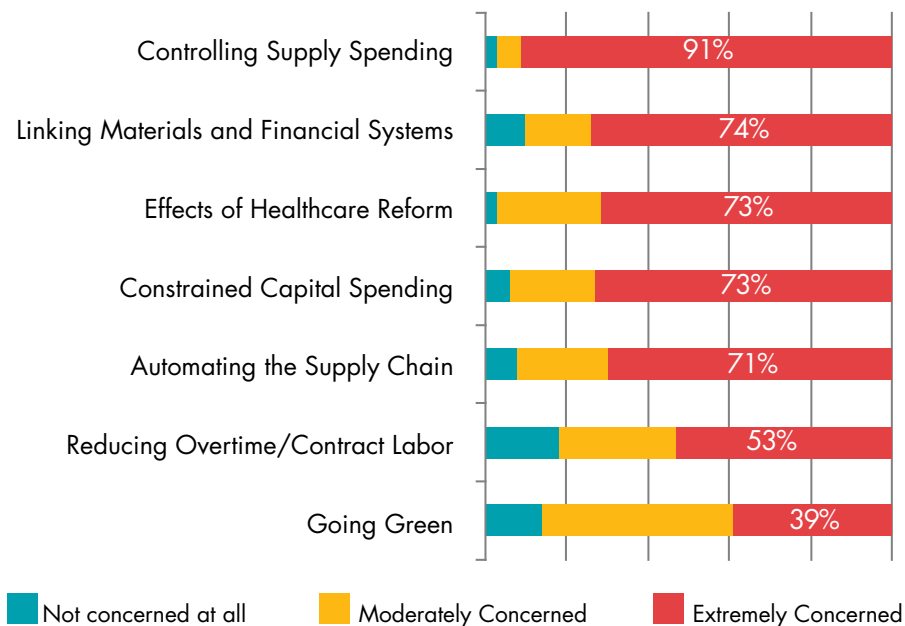
*"My world/job is consumed by implementation of the Consolidated Service Center. Everything else is dwarfed by that."*

*"Effect of never events and evidenced-based decision-making on the selection of products."*

*"Adoption rate of GS1 (product tracking) standards, spend analytics enhancements, regional sourcing collaborative contracts, life cycle management."*

*"Ability to get to a more strategic level with key stakeholders, including GPO. Rather than just talking about price, (we need to achieve a) better understanding of the total cost/benefit of decisions."*

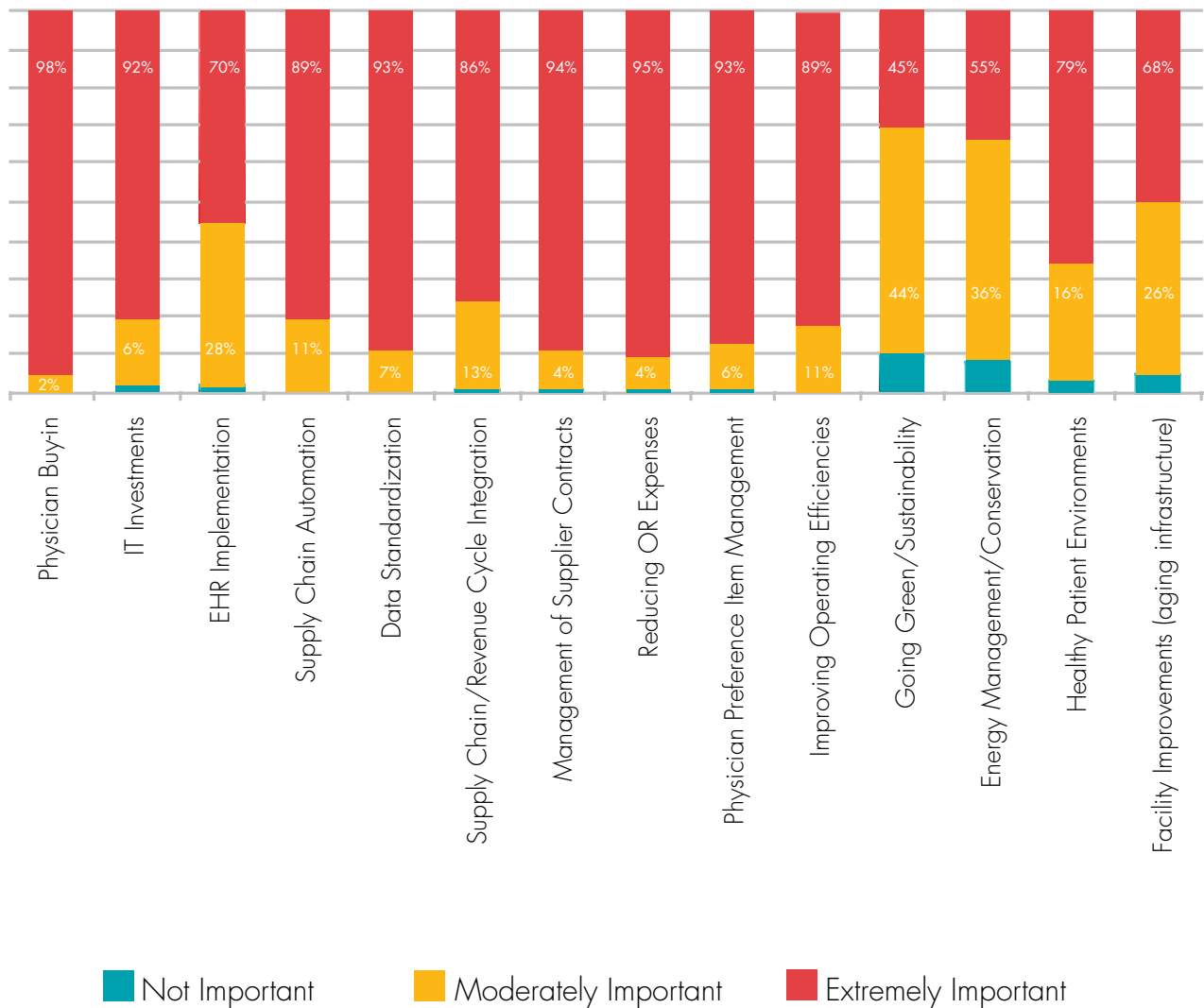
### Areas of Concern in Daily Operations



## AREAS OF STRATEGIC IMPORTANCE

We asked supply chain management professionals to identify the strategic importance of 14 components of the supply chain function. Physician buy-in had the highest percentage of respondents saying it is “extremely important” to the supply chain function. Physician preference item management, management of supplier contracts, data standardization, reducing operating room expenses and improving operating efficiencies also scored highly. Going green and energy conservation ranked lowest in strategic importance among respondents, presumably because of the dedication necessary to the higher-priority supply chain function, although many facilities are already implementing some basic strategies within these areas.

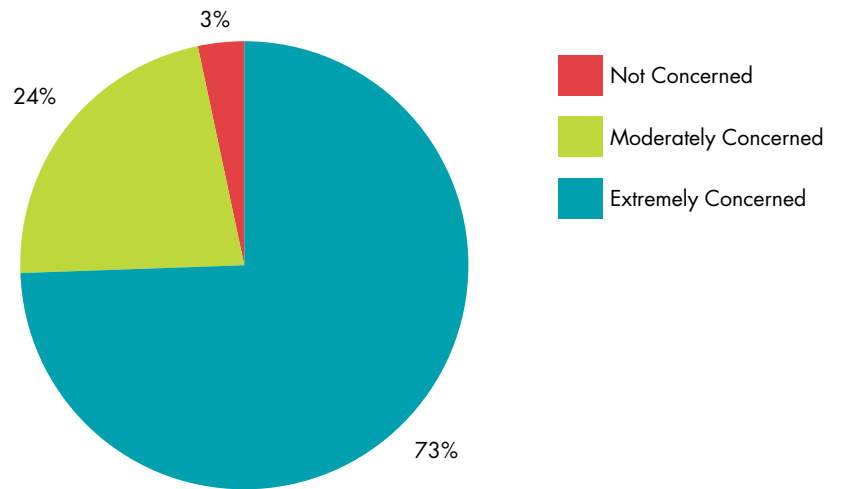
Importance of Various Aspects of Supply Chain Function



## HEALTHCARE REFORM

The whirlwind of healthcare reform proposals being discussed in Washington was clearly of major interest to respondents, with 97% expressing at least moderate concern with the potential of reform to affect the industry. As the reform legislation wound its way through Congress, at least \$400 billion in provider payment cuts—including \$155 billion in lower hospital reimbursement—was foreseen over 10 years to help pay for broader reforms related to coverage. Moreover, a new Independent Medicare Advisory Board is likely to be created by any legislation, raising the prospect of even further payment reductions and/or new regulations governing the hospital industry. This impetus has put more pressure on the supply chain executive to achieve an optimized, transparent supply chain.

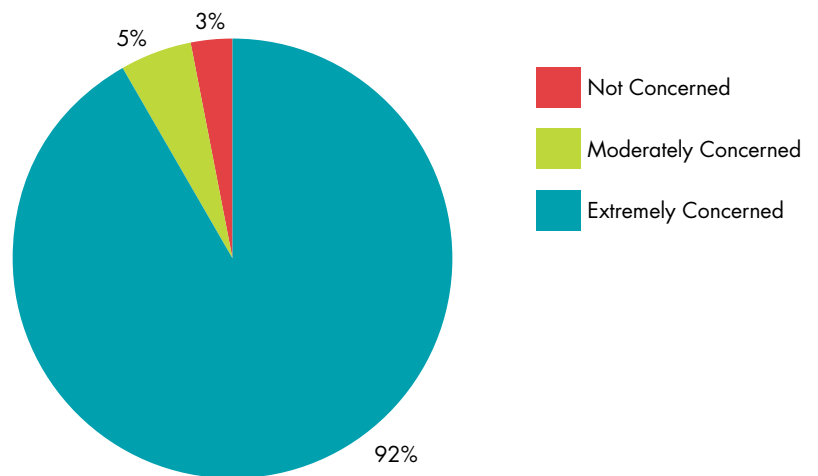
Concern With Effects of Healthcare Reform on the Supply Chain



## CONTROLLING SUPPLY SPENDING

Not surprisingly, controlling supply spending is another top-of-mind issue for these supply chain management professionals, with 97% of respondents at least moderately concerned with it. There are many solutions, led, of course, by utilizing group purchasing organizations, with 94% of respondents belonging to one or more GPOs. However, this survey report details plans by many systems and IDNs to try other means of lowering costs, with some citing problems with price transparency among the GPOs. About three quarters of respondents are doing some direct contracting with suppliers.

Concern with Controlling Supply Spending



A more novel approach is vendor managed inventory, a lean distribution strategy common in non-healthcare industries but now picking up appeal in healthcare. About a third of respondents have already adopted the strategy, with 24% planning to implement a project in one to three years. More than half of respondents report either having started or readying plans to jointly manage inventory with a vendor.

Many respondents have turned to regional buying cooperatives for medical-surgical supplies, with 43% already participating and 19% planning to do so within three years. A similar strategy is consolidated service centers, which are jointly owned and managed by multiple hospitals and healthcare systems and bring together geographically based groups of hospitals. CSCs centralize contracting, procurement, distribution, logistical operations and customer service. About half of respondents are investing in them.

Of course, some GPOs have invested significant resources developing programs and value-added services to better differentiate themselves from other buying groups.

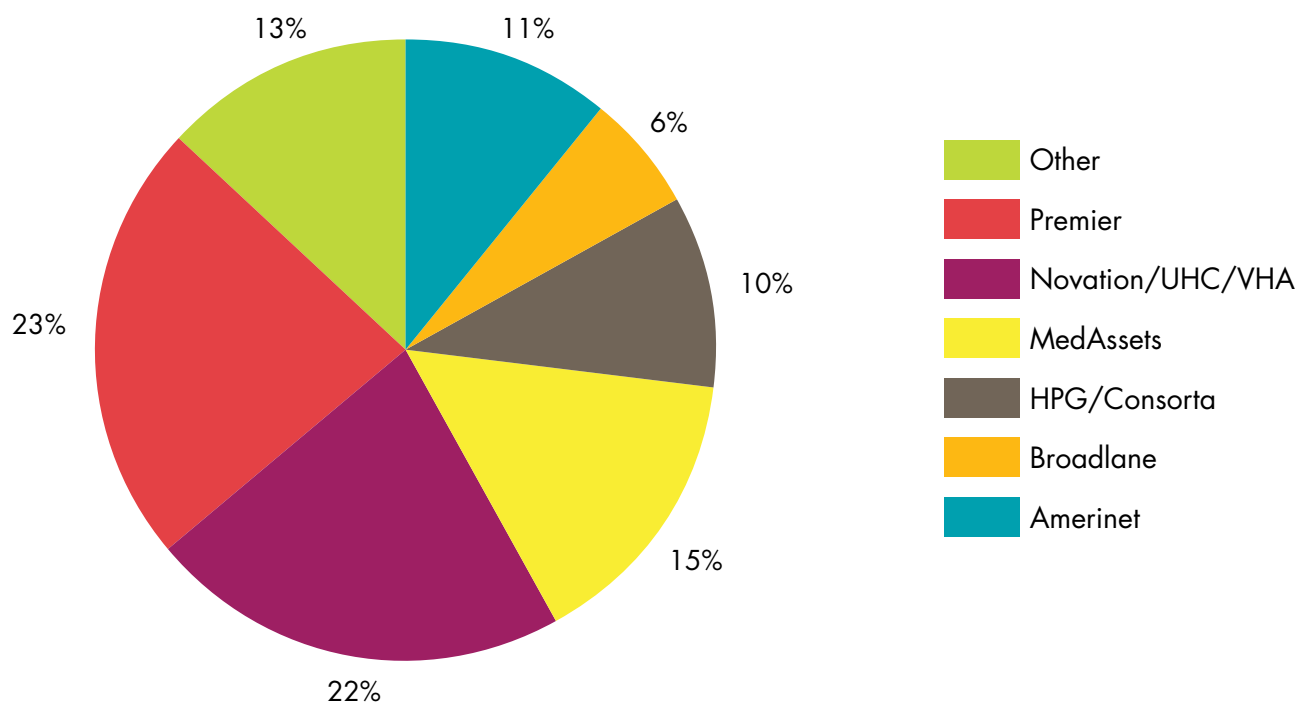
Other strategies mentioned include IDN self-contracting, local contracting for physician preference items and governmental cooperatives.

## GPOS: A SNAPSHOT OF USE

Just 27% of respondents say they buy 75% or more of their purchases through GPOs, though another 41% report buying from half to three quarters of their supplies that way. Just 4% said they buy less than 25% of supplies through a GPO. Below is a breakdown of respondents' GPO affiliations.

Simply belonging to a GPO and buying the vast majority of materials through that contract seems to be an exception to the rule. When asked what other strategies they are implementing beyond GPO contracting, we received a wide range of replies. A number of respondents indicated belonging to multiple GPOs, and using various means to extract greater value from the GPO. As one wrote on the survey: "(We have) obviously a multiple GPO sourcing strategy, coupled with a prime vendor arrangement and exclusive contracting where we can materially reduce the GPO pricing."

### Respondants' GPO Affiliations

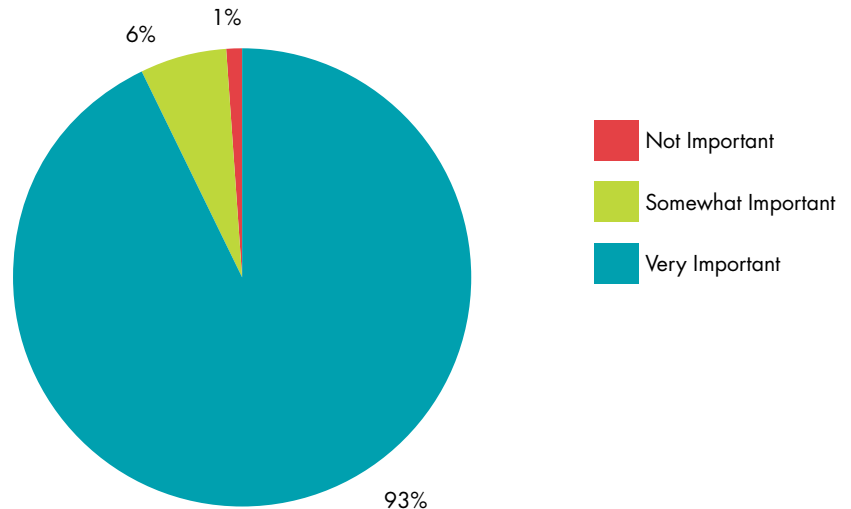


## MANAGEMENT OF PHYSICIAN PREFERENCE ITEMS

One of the most longstanding and challenging issues that healthcare systems face in controlling supply costs is the complex process of assessing, selecting and purchasing physician preference items (PPIs). Physicians often express strong preferences about which supplies they wish to use during surgery, often without regard to cost or the fact that having multiple types of product packages on hand reduces the ability of supply managers to negotiate discounted prices.

Physician preference items have been receiving increased scrutiny since the beginning of the current recession. High rates of product expiration, lost product revenue and the headaches of the current consignment-based model have led many supply-chain managers to call for innovation in the management of these products. Many hospitals that have been reluctant to approach their physicians on PPI are now doing so. There are several key strategies currently employed.

Strategic Importance of Physician Preference Item Management



### Value Analysis Teams

One collaborative approach to product selection is technology assessment and/or value analysis committees. Value analysis teams are the most commonly implemented PPI strategy cited by respondents, with 73% having already implemented it. Materials managers hoping to standardize on physician preference items, especially at the IDN level, need to understand the mindset of clinicians. In order to do this, many hospitals set up cross-functional teams to evaluate new products and equipment and to review currently utilized products and equipment. The range of professionals that serve on these committees varies from hospital to hospital, and in some cases does not include physicians. The goal of these teams is to ensure that products and equipment meet the requirements for providing quality patient care, while supporting product standardization and cost containment initiatives of the institution. Many hospitals are seeking to strengthen these committees so that products can be better evaluated for both their effectiveness and cost. As pressure on financial margins increases, and as the role of products is better recognized as a contributing factor in patient safety issues, these committees are becoming increasingly important.

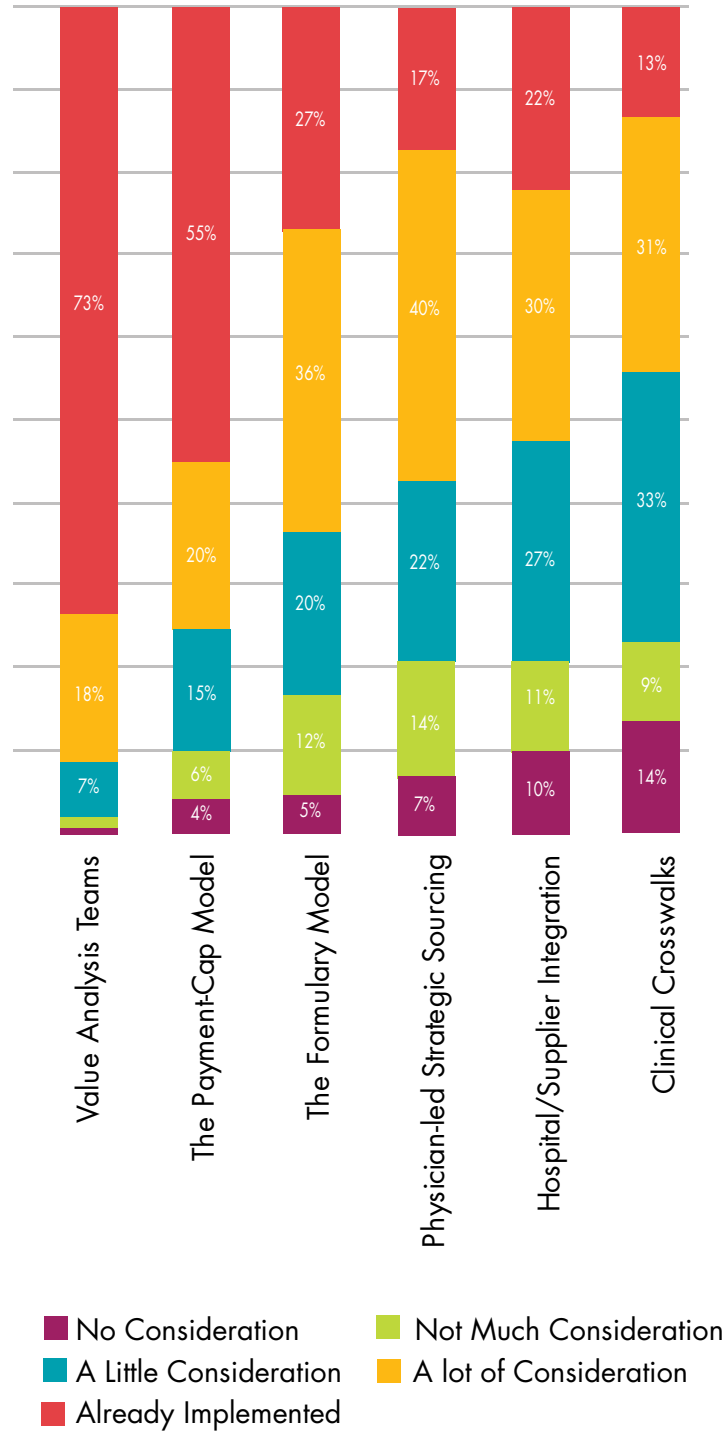
### The Payment Cap Model

Another common PPI strategy is to impose price ceilings—known as the payment-cap model—with 55% of respondents having already implemented this strategy. In this model, the provider establishes price ceilings on item categories, regardless of the vendor. Hospitals using a payment-cap method expect competition between multiple manufacturers to offer equivalent products within the hospital's price ceiling for each device. Theoretically, the payment-cap method forces the vendor, rather than the physician, to adjust to hospital spending restrictions, thus allowing physicians to freely select supplies without focusing on the cost component as heavily.

### The Formulary Model

The formulary model is a PPI strategy where the hospital commits to a single vendor with the expectation that it will offer the hospital lower prices. In this strategy, value analysis teams create a list of products by category that are both clinically and cost-effective, and require physicians to choose between products on the formulary. This allows materials managers to increase the reliability of demand forecasting and reduce the costs of supplies through economies of scale. This strategy requires strong commitment from physicians, since it requires them to make choices on products that fall within the formulary.

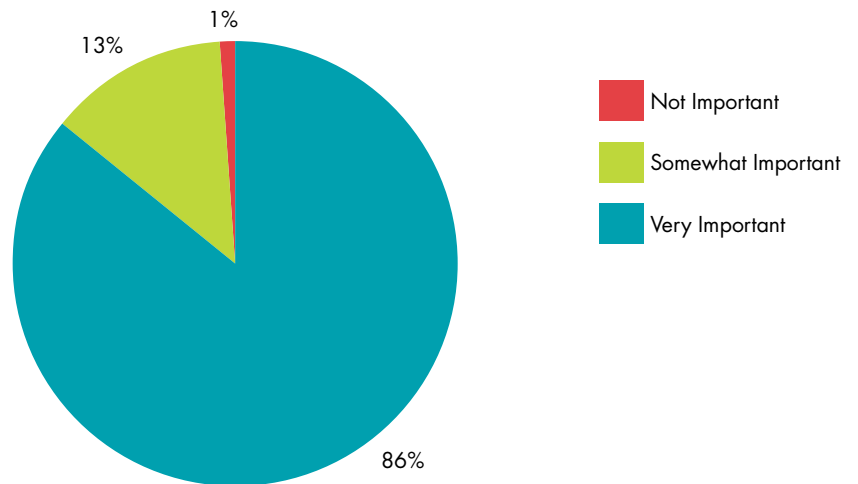
### Level of Consideration for Various Physician Preference Item Strategies



## LINKING MATERIALS AND FINANCIAL SYSTEMS

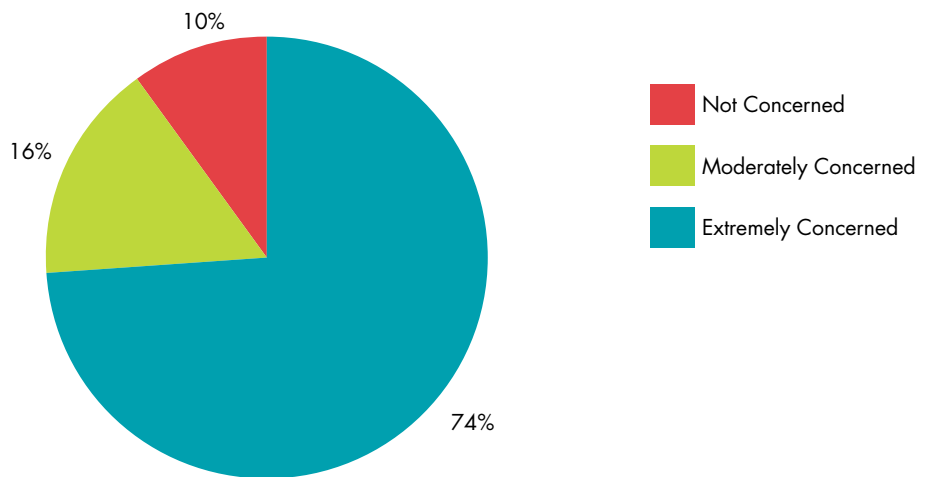
One of the key pieces to managing the revenue cycle is the link between the cost of products and the price being charged. Understanding how billing and payment accuracy can affect the margin associated with reimbursement for supplies can lead to better contracting strategies and profitability. More and more, supply chain leaders have the opportunity to enhance their organizations' ability to maximize revenue cycle expectations while lowering the expenses associated in procuring supplies and technologies. Most of those surveyed said that linking the supply chain to the revenue cycle is a serious concern.

Strategic Importance of Supply Chain-Revenue Cycle Integration



There is a disconnect in hospital accounting of supplies. The supply chain side of the hospital operation uses the facility item master—the inventory of every supply that a hospital uses. In the finance department is found the charge master—the list of every procedure, service and supply that a hospital can charge to patients, along with the appropriate coding information and the price to be charged.

Concern with Linking Materials and Financial Systems



The price of many items fluctuates based on supply and demand, making it difficult to ensure the item is appropriately charged, resulting from disparate supply chain and revenue cycle systems. The heart of the problem is found in the fact that the departments use different information systems. Because of this, collaboration between materials and finance has increased dramatically over the last five years. This revenue and supply cost linkage is especially important for hospitals that receive reimbursement on a percentage-of-charge basis. When negotiated using actual supply cost data, these contracts can provide hospitals with the cost plus some mark-up for any high-cost devices used.

## PROCESS IMPROVEMENT

A move toward continuous quality improvement across the healthcare enterprise has picked up steam over the past decade or so. All stakeholders are concerned about the quality and cost-efficiency of care. Media attention and government intervention on medical errors—fueled by a series of reports from the Institute of Medicine—have also prodded healthcare providers to adopt the leading quality improvement systems. The goal is eliminating some of the variability in treatments, eliminating the causes of common errors and finding new efficiencies. With new pressures on reimbursement, it is no wonder that our survey found significant interest in and action on process improvement.

Fifty-four percent of respondents had already implemented Total Quality Improvement, Lean or Six Sigma in the supply chain/materials management area, and 23% plan to do so in the next few years. Fully 89% of respondents view improved efficiencies as extremely important to their operations.

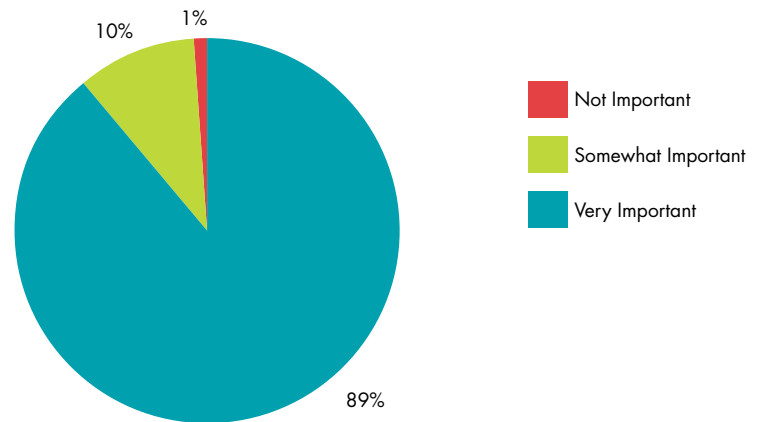
## CONSTRAINED CAPITAL SPENDING

With credit markets tight and capital for purchases held at a premium, managing capital acquisition and utilization as well as non-commodity supply costs has become one of the leading areas of focus.

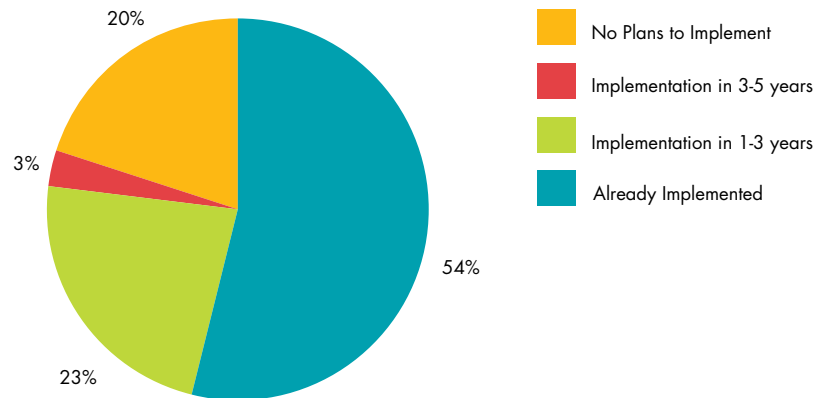
Many hospitals have cut capital spending for facility upgrades, clinical technology and/or information technology. These projects include renovating and updating aging facilities, expanding clinical technology available to the hospitals served or expanding access to existing services.

According to the American Hospital Association, 31% of hospitals reported that their ability to access capital has decreased since December 2008. This is in line with the survey results, in which 73% of respondents expressed extreme concern with constrained capital spending.

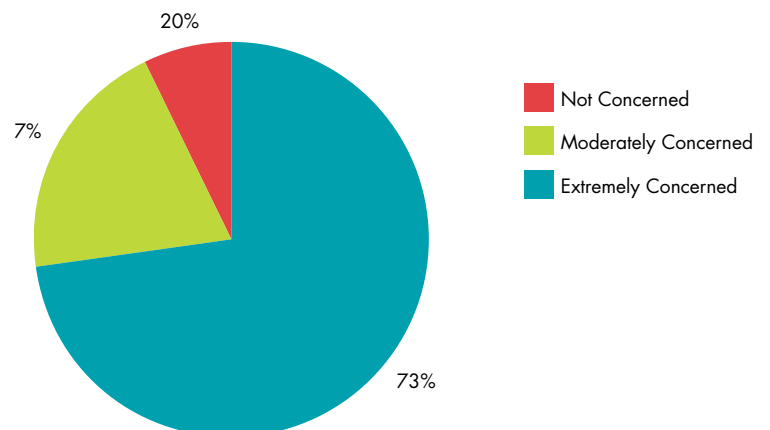
Strategic importance of Improving Operating Efficiencies



Implementation of Quality Management Programs



Concern with Constrained Capital Spending

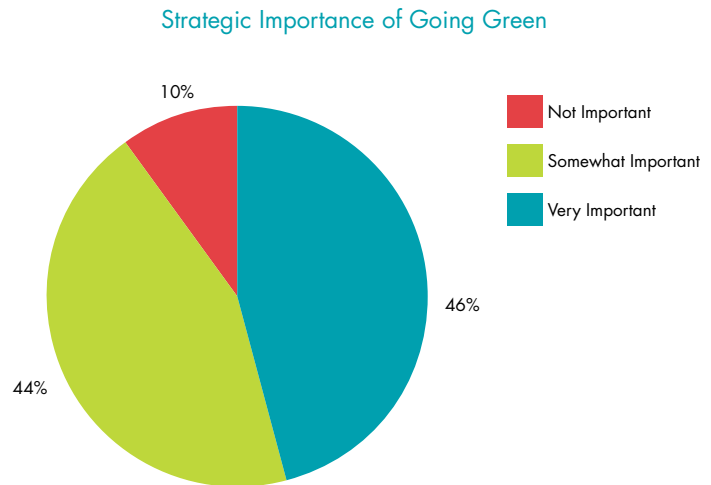


## GOING GREEN

Over the past decade, a move toward environmental sustainability in the healthcare supply chain was clearly afoot. Our survey at first glance appears to contradict that impression, with “going green” ranking at the low end of the top concerns of respondents. When we dug deeper into the responses, however, we found the situation a little more complicated, with substantially more interest and/or action on the environmental front.

Those interests included:

- Reducing volatile organic compounds—chemicals emitted as gases from liquid or solid products such as formaldehyde (found in some types of building materials, permanent press drapes and paint), pesticides, solvents and cleaning agents. These gases are often toxic to the liver, kidneys and central nervous system. Thirty-nine percent of respondents said they had given the issue a lot of consideration, and 15% had already adopted programs to reduce the compounds.
- Recycling or reducing the use of single-use devices. More than half of respondents now recycle the devices, and 54% either had implemented or were strongly considering programs to reduce their incidence.
- Forty percent of respondents were giving a lot of consideration to sustainable construction, the practice of creating structures and using processes that are environmentally responsible and resource-efficient throughout a building’s lifecycle. Another 18% had already implemented a “green construction” program.



In something of a surprise, a process widespread in many industries—LED lighting retrofits—is not a priority of respondents. Just 16% said they had done a retrofit and 29% were strongly considering doing so. Because healthcare facilities operate 24/7, about half of their energy consumption comes from lighting. Studies have found savings from lower energy use in energy efficient LEDs, along with available tax credits and reduced maintenance costs due to longer life of the bulbs.

There were a number of remarks on the survey responses indicating that though respondents were well aware of environmental needs, they lack the budgetary resources to advance those programs.

## CONCLUSION

This baseline survey presents a useful first step toward a more complete understanding of the dynamics of the healthcare supply chain as well as opportunities for improvement and the challenges faced when attempting to achieve improvements. The data show that supply chain professionals have a range of tools to lower costs and improve quality. To the extent that they are able to exert influence on other departments, such as with physician preference items and medical-surgical supplies more generally, supply chain leaders can play a major role in healthcare organizations’ efforts to maintain financial variability in a highly volatile time in the industry.

Reading individual comments on the survey forms, we also note frustration among many respondents with budget cutbacks that affect personnel and technology improvements, some trouble gaining the ear of senior leadership and continuing struggles to keep vendor pricing under control.

Perhaps this data can help begin some new dialogue about the importance of the supply chain in helping the healthcare industry deliver safer and more cost-effective patient care.

The logo for IDN Summit and Expo features a stylized circular icon on the left, composed of overlapping curved lines in shades of blue and orange. To the right of the icon, the text "IDN SUMMIT" is written in a large, bold, blue sans-serif font, and "AND EXPO" is written below it in a smaller, orange sans-serif font.

# IDN SUMMIT AND EXPO

## *About IDN Summit and Expo*

*Since its creation in 1986, IDN Summit and Expo has become the leading source of collaborative networking events, education and information resources and professional services for healthcare supply chain stakeholders. It focuses on best practices, enhanced communication and improved business processes that lead to more cost-effective patient care. The spring and fall summits bring together senior healthcare executives and their group purchasing organization and supplier partners in an open, learning environment. The meetings have as their foundation a range of strategic content developed by an independent Educational Advisory Board made up of senior integrated delivery network executives. Additional information may be found at [www.idnsummit.com](http://www.idnsummit.com).*



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September 21-23, 2010

Healthcare Business Media, Inc., dba IDN Summit & Expo  
2201 Regency Road, Suite 302, Lexington, KY 40503  
P 859-523-5701 F 859-523-5799 [www.idnsummit.com](http://www.idnsummit.com)