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**Healthcare Excellence Institute**

**The Science of  
New Revenue Cycle Thinking**

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## Gaining access to the biggest source of additional cash – the revenue cycle

Even after, or maybe because of many years of driving incremental and evolutionary change in revenue cycle operations, revenue cycle operations present the single biggest immediate financial leverage point for provider organizations. The empirical evidence suggests that even the best run revenue cycles experience a cash leakage of approximately 4% of net revenues, with the typical leakage being approximately 8%. In an industry struggling to achieve margins above 3-4%, capitalizing on this leakage can take many organizations from the brink of financial disaster to break even or prosperity in a short amount of time.

Many financial and revenue cycle leaders still live in daily denial of the very possibility of large untapped potential within revenue cycle operations. The argument typically portrayed is, *“if incremental improvement and change has been taking place for decades, then the revenue cycle has been tapped.”* It is simply incomprehensible that such a large opportunity remains untouched. This argument though is analogous to the paradigm of producers of buggy whips at beginning of the last century. While the buggy whip example is more self evident in retrospect, the revenue cycle parallel has only reached the equivalent comprehension with the most visionary leaders in the industry.

One example that highlights the possibility of this revenue cycle reality - ***that very large sums of cash are in fact not realized by provider organizations*** - is the proliferation of extended business office services and the existence of many highly profitable collection agencies servicing this market. Revenue cycle leaders should ask themselves the question:

*If the revenue cycle is performing optimally, then why do so many back-end service providers exist, and flourish, generating net operating margins that far exceed those of the provider organization generating the original accounts receivables?*

The reality, of course, is that the hospital revenue cycle is sub optimized. Healthcare’s cost center mentality and budget orientation has resulted in antiquated processes, siloed organizational methods, and this logical, but incorrect approach, of incremental improvement. All of these factors combined have birthed an entire industry of highly profitable servicing companies.

## The highest revenue cycle cost is not what traditional wisdom suggests

Labor is usually considered the highest cost in any hospital revenue cycle. During times of financial hardship, this component is the one receiving the most scrutiny and activity. However, when looked at more holistically, after shedding the constraints of cost accounting viewpoints and the associated departmentalization of costs, the greatest cost in any revenue cycle, even the best ones, is ***unrealized net revenues***.

This one line item ‘cost’ dwarfs any other cost associated with the revenue cycle by a multiple. It rarely receives the attention it deserves, however, because it is hard to see through the convoluted construct of bad debt reserves plus recoveries based on cryptic and often interpreted and adjusted look-backs.

One counter argument that is often raised to this point is the inevitable loss of cash realization associated with the uninsured population. While there is some truth to this statement, we cannot argue with the very real cash realization losses that occur in the insured population, which is a conservative estimate of a hospital's true opportunity. Figure 1 - the True Revenue Cycle Cost Comparison – clearly illustrates these points. This data is based on the actual functioning of large number of hospital facilities.

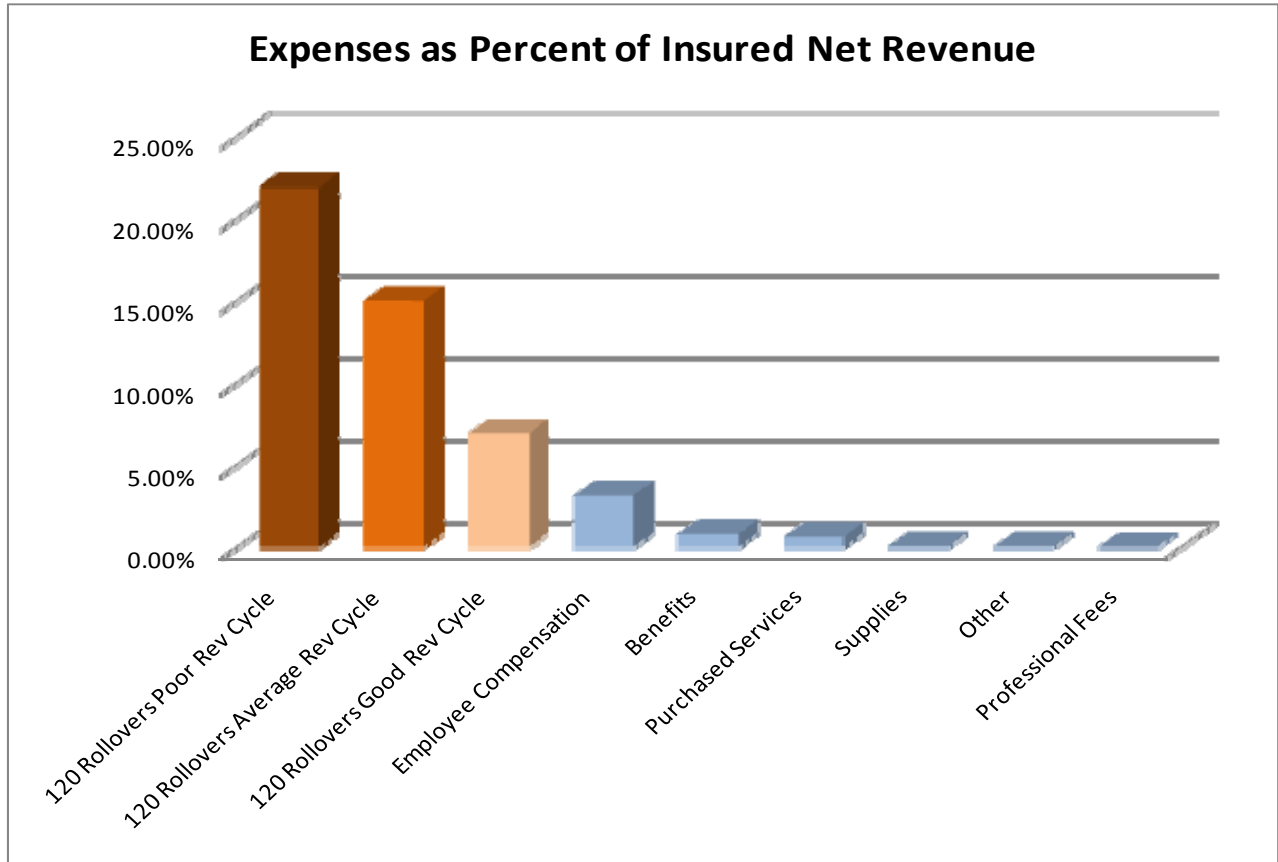


Figure 1 – True revenue cycle cost comparison

Another counter argument often recited by revenue cycle traditionalists is the ‘evidence’ provided by mediocre recoveries returned by the collection agencies once the accounts have been outsourced. This argument however lacks the understanding of life cycle properties of healthcare accounts receivables. It is often discussed and recited that collectability decreases as accounts age, but rarely is a precise number placed with this phenomenon. When conducting empirical research across many provider organizations, with different revenue cycle performances, the evidence and its valuation become clear. In order to understand the impact of aging, a large account pool (several months of inventory) must be tracked vis-à-vis aggregating cash receipts over a time line starting at the discharge date of each account and comparing those cash receipts against the net revenue. When this analysis is conducted across many providers, a clear picture emerges:

## Cash Realization Profiles

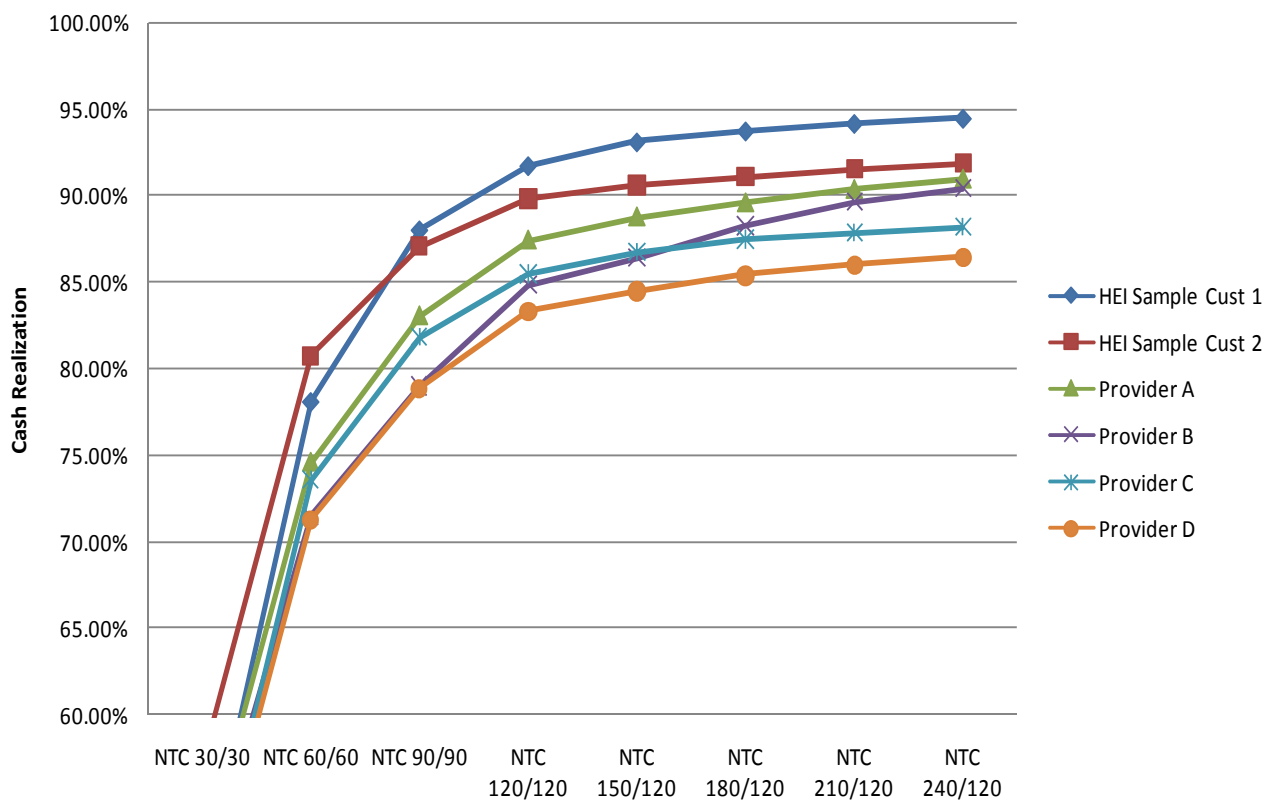


Figure 2 – Life cycle reality of accounts receivables

Once accounts age to about 120 to 150 days post discharge, their cash realization profiles become asymptotic and the revenue cycle leakage has ultimately already been determined. Follow up activity at this point in time becomes somewhat of an exercise in futility given the opportunity that has already been lost. A pattern of loss or potential additional cash realization is actually established very early on in the life of an account, with the cash realization performance of 90 days post discharge being an excellent predictor of the ultimate financial outcome.

What this finding indicates is that ‘cash acceleration’ is in fact much more than accelerated cash flow. Its value goes well beyond the time value of money. There is a direct cash and net income impact in a one to one relationship, rather than vis-à-vis a delay in cash flow valued at the weighted average cost of capital.

Reducing this leakage requires a multifaceted approach to managing and changing the traditional revenue cycle operations. A cohesive and modern system must be implemented to capture these opportunities.

## **Implementing a Management System**

The primary step that must be taken is the implementation of a true revenue cycle management system. A management system entails many different components - the keys, however, are: 1) a precise measurement system and 2) a standardized corrective action system used throughout the organization. We have already outlined that the traditional methods of measuring revenue cycle performance are woefully inadequate to pinpoint revenue cycle leakage in a precise fashion, and the traditional metrics of Net as a Percent of Cash, Net AR days and Total Cash receipts are only counterproductive and a hindrance to higher levels of performance. Secondly, the new generation measurement must be joined with a managerial corrective action system embraced and followed by the entire organization such that the new information is translated into meaningful action.

## **Organizational Design for Success**

Another item that must be addressed is organizational design and development. In a world of increasing payer and regulatory complexity, the sweatshop mind set, where hands are hired to do a job, is no longer relevant. The development of a true high performance organization, leveraging High Performance Work Teams (HPWTs), with all of its elements becomes imperative to success. High Performance Work Teams are cross functional, its members are physically co-located and held accountable collectively. They are provided with the tools, leadership and transactional support needed to be successful in a reality of high complexity.

## **Process Change that considers Psychology**

Furthermore, a repeatable method of process change, one that not only changes processes but addresses the cultural issues associated with process change adoption, the cultural component, must be introduced to turn newly gained knowledge into results. Culture change, often belittled by the technically educated ranks, is one of the most critical pieces often left out of the discussion when attempting to drive change. The knowledge base derived from research around the topic of psychology of change has to be considered as processes are changed within the revenue cycle.

## **The Role of Technology**

Lastly, technology is a consideration in moving the revenue cycle to a new level of performance. Many useful technologies are being introduced to the market that should be used to supplement the outdated HIS modules. That said, technology should not be turned into the driver of change, but rather a supporter of change. This is especially true in highly competitive environments. Purchased technologies can never become a strategic differentiator since it is available to all market participants. Sound processes, a tight management system and a high performance culture however are hard to replicate and thus become the bedrock of competitive advantage, as has been demonstrated by organizations such as Toyota Motor Company and Southwest Airlines.

In summary, much opportunity remains for most provider organizations to change the financial outcome of their organization by addressing and rethinking revenue cycle operations. The value proposition is unparalleled in comparison to other initiatives that could be conducted and in times as these, transforming the revenue cycle may well be the best option.

## **Comprehensive Alternative Revenue Cycle Business Model**

In 2003 HEI and CHRISTUS HEALTH, HEI's revenue cycle development partner, set out to create a world class revenue cycle business model. Our success in reaching this goal has now been continuously confirmed since 2005 as evidenced by a series of awards such as the best revenue cycle (PFB awards) in 2009 from HFMA, the 2010 HFMA MAP award, the Global Six Sigma Award and two Six Sigma Excellence Awards. In addition to these awards the principles and practices have been recognized as benchmark in many industry audits such as the ones conducted by JCAHO. The financial outcomes generated have led to an increase in cash from net revenue of up to 12%.

This achievement is the result of implementing an integrated business model that encompasses a unique management model, non-traditional organizational structure, flow based processes and patent pending supplemental technologies. These components and their integration have defined a new type of revenue cycle business model that not only delivers unprecedented financial results, but also creates a culture and processes that thrive on change and improvement.

## **Healthcare Excellence Institute -- Contrarian Revenue Cycle Solutions for a New Reality**

Healthcare Excellence Institute was founded on the premise that substantial additional cash will be generated by applying non-traditional methods to revenue cycles.

HEI's product and services portfolio offers solutions for customers ranging from those needing a limited scope solution, to those desiring a comprehensive revenue cycle redesign and to organizations desiring to outsource the entire revenue cycle.

Samples of our Product and Services Portfolio:

- **Comprehensive Revenue Cycle Transformations**
- **New Generation Revenue Cycle Scorecard & Management System (ScoreLogix™ -- ASP Software)**
- **Extreme Makeover Events (Consulting)**
- **Scientific based Collections Optimization (CollectLogix™ -- ASP Software)**
- **High Performance Organization (Consulting)**

**HEI has used its 10-year experience of applying Toyota Production Systems / Lean Six Sigma with Fortune 100 companies and applied this expertise to healthcare business operations. It was founded in 1997 and is headquartered in Phoenix, AZ. HEI's healthcare clients have won multiple international awards for their world-class onsite business processes.**