

Materials management

How ORs track, manage supply costs

Before an OR team can control its costs, it needs to know what they are. This year's *OR Manager* Salary / Career Survey asked managers what they use as a cost indicator for surgical supplies (related article, p 9).

In interviews, 4 OR business managers discussed indicators they use and how they employ them in making decisions and controlling costs.

University of Wisconsin, Madison

30 ORs (22 inpatient, 8 outpatient)

22,000 procedures a year

Supply cost indicators used at this academic medical center include:

- supply expense per case
- supply expense per OR minute
- implant cost per case
- implant cost per OR minute.

The first 2 indicators, kept on a spreadsheet, are calculated by dividing the supply expenses from the OR's monthly operating statement by the number of cases and OR minutes for that month. The result is an average supply expense per case and minute.

"We monitor that to watch for trends," says Katherine Hurtgen, MBA, OR business operations manager.

Scorecard monitors trends

A new automated scorecard gives managers a user-friendly tool for monitoring financial health and other indicators (illustration, p 13). Indicators are coded green for on target, yellow for out of range, and red for "Stop, we have to find out what's going on." Red requires a report to senior administrators.

"It's a simple tool to look at," says Hurtgen. "We've been tracking these measures all along on spreadsheets. Now we can just pop into the system and see how we're doing." The management team sets the goal and variance range for the indicators. On expense per case, for example, the indicator turns red if the figure is more than 10% outside the average for a given month. The scorecard software is from ActiveStrategy (www.activestrategy.com).

Implant expense per case is calculated by marrying data from the purchasing system with case records from the OR information system.

If there's a spike in supply costs for a given month, Hurtgen digs deeper. She might review implant usage to see if that is driving costs. Recently, the culprit has been ventricular-assist devices (VADs), which cost about \$73,000 each and serve as a bridge to heart transplant.

Cost analysis is becoming more robust with the recent installation of a PeopleSoft purchasing system, interfaced with the OR system, GE Centricity Perioperative.

"This can give us the price per unit for all items listed on the preference card for a case," Hurtgen says. "I can get cost-per-unit at the end of a case pretty easily."

The biggest glitch has been the difference in the unit of measure of supplies ordered and used.

"When we first went live, I was looking at the data and saw a \$1,200 stapler—it was really a box of 6," she says. Though she says she is about 90% confident of the data, "before I hand a report to a surgeon, I want to be 100% confident."

**St Joseph Hospital,
Orange, Calif**

27 ORs (14 main OR, 13 outpatient)

25,000 procedures a year

Two indicators managers rely on most:

- supply cost per OR minute
- average implant cost per case.

"My goal is to keep the supply dollars per unit of service the same. If we do more minutes than budgeted, we will obviously spend more, but if the dollar amount per unit of service is roughly the same, it's justifiable," says Terrence Wooten, OR business manager.

Supply cost per minute is also a target for the staff incentive program. Staff can earn a bonus for, among other things, lowering supply cost per minute by 2%. (See September 2005 *OR Manager*.)

Wooten also tracks the cost per case of high-cost implants, looking for trends. For example, if the hospital has negotiated a contract for better pricing, he expects to see a decrease.

He monitors the budget using monthly variance reports, though these aren't available from the finance department for about 3 weeks after the end of the month. For quicker feedback, Wooten gets a report from the materials coordinators on that month's purchase orders.

"We try to track those week-to-week so there are no surprises," he says. "Depending on where we are for the month for purchases that aren't patient related, we might say, 'Do we need this now? Or can we get it later?'"

The cost data is also used in making decisions about new products.

"When surgeons want new items, we look at the cost of the procedure with and without the item. We also look at the reimbursement, net revenue, and what the gross margin would be if the supply is added," he says.

**Highline Medical Center,
Burien, Wash**

9 ORs

5,400 procedures a year

At this community hospital in suburban Seattle, the major productivity measure is the OR minute. Supply cost indicators are:

- total expenses/case
- supply expense/case
- supply cost/OR minute.

Krista Christensen, MBA, CPC, business manager for surgical services, compiles a financial summary each month using those indicators, getting most of her information from the budget report.

The summary is shared with the director of surgical services, chief nursing officer, and controller.

Every month, a budget variance meeting is held, which departments that are over budget must attend.

"For us, it is usually the supplies that are off," particularly expensive items like total joints, Christensen says. In June, for instance, the total joint volume doubled in one month, which threw the expense per OR minute off.

Christensen keeps track of areas she knows will affect the budget so she can provide a rationale.

"I look at any new services we didn't budget for, whether we've had a spike in our volume, and whether the value of the inventory on the shelf has increased," she says. For example, late last year, the hospital introduced cryosurgery of the prostate, which carries a large supply expense. The cost wasn't included in the 2006 budget, which was already completed.

"If we are over budget, I can work back and say, 'These are the things that con-

tributed to it," she says. "We brought in a new service, and they tend to forget there is going to be a budget impact."

Shands Hospital at the University of Florida, Gainesville

26 ORs

16,000 procedures a year

Like many others, Shands uses supply cost per case as an indicator.

"We see it rise every year. It's almost entirely due to technology," says Fred Buxbaum, OR business manager.

Some of the biggest challenges are high-cost implants such as InFuse (bone morphogenic protein used in spinal surgery), vagus nerve stimulators, and cochlear implants.

But it's about more than costs—a variety of factors affect whether a procedure is profitable, Buxbaum stresses.

At Shands, an Implant Committee was formed last year to look at the broader issues of managing these expensive items. Members include a representative from administration, who chairs the meetings and reports directly to a vice president, and personnel from the OR, information services (IS), purchasing, and reimbursement.

In addition to costs, the committee examines:

- Who are the payers? What is the profitability for each of the major payers for an implant procedure?
- Is there a difference in inpatient and outpatient reimbursement? "For certain types of implants, we are better off having the procedure done on an outpatient basis if appropriate and being paid under the APCs," Buxbaum says, referring to the ambulatory patient classifications Medicare uses for hospital outpatient payments.
- Is the chargemaster set up correctly for these procedures?
- Is the procedure being coded and billed correctly?
- Is it a pricing issue? The hospital may need to negotiate better prices for some products.

"By gathering the data and having the right people at the table, you're able to formulate a plan that results in improved profitability for your hospital," Buxbaum says. ❖

'Checkbook' controls instrument spending

A "checkbook" approach helps keep instrument spending in line at St Joseph Hospital in Orange, Calif.

Each OR service line manager has a monthly instrument budget (the yearly budget for the service divided by 12), which he or she uses like a checking account.

"They have the choice of spending it all in 1 month or banking it and spending it later. We track it month-to-month," explains Terrence Wooten, OR business manager.

"It's caused them to focus on what they are spending and project their needs. This has been working very well for the past 2 years."

Tips for tracking supply costs

Advice from OR business managers on monitoring and managing the cost of supplies.

Understand the OR budget

Before you can start using supply cost indicators, you need to understand the

OR budget—where do the numbers come from, and is the budget an accurate reflection of the department's financial situation?

That's the advice of Terrence Wooten, OR business manager at St Joseph Hospital, Orange, Calif. He says it took him 2 years to develop a thorough understanding of the budget.

"Once I was comfortable with the budget, and we had a good process for working together, I was more comfortable looking at supply costs," he says.

Develop a metric you can track

Work with your accounting department to develop a metric for supply costs, suggests Katherine Hurtgen, MBA, OR business operations manager at the University of Wisconsin, Madison.

A simple metric is surgical supply costs divided by the number of surgical cases or OR minutes.

"That gives you a metric to keep an eye on," she says. "You don't need a fancy system to do this. It can be kept on a spreadsheet. You can break it down by month and track it going forward."

If the indicator spikes—say you're typically at \$11 per case and it jumps to \$15—it's time to investigate. Dig into your purchase orders for the past month and ask, "What are we ordering more of that we didn't used to?" she advises.

Look beyond costs

Managing the supply budget is about more than tracking costs. Costs rise each year. But is your revenue keeping up? How's your profitability? Are you coding and billing procedures correctly?

"You have to dig deeper to find out what's going on," says Fred Buxbaum, business manager for the ORs at Shand's Hospital at the University of Florida, Gainesville.

He enlists support from coders, billers, reimbursement specialists, clinical experts, and information systems to get the information he needs to help the organization's decision makers see the big picture.