

HOSPITAL OUTSOURCING TRENDS IN CLINICAL SERVICES

A SURVEY SPONSORED BY Waller Lansden Dortch & Davis

According to Reggie Hill, head of the nationally recognized healthcare practice at Waller Lansden Dortch & Davis LLP: "Waller Lansden sponsored this survey because we understand that many hospitals are making the decision to outsource one or more clinical services, and we believe that such decisions should not be made in a vacuum. Because most outsourced services are not separately licensed, it is difficult to gather any data as to either the prevalence of hospital outsourcing or the types of clinical services being outsourced. In an evolving market, this survey is intended to set benchmarks against

which future trends and developments can be measured."

RESPONDENT PROFILE

The *2006 Hospital Outsourcing Trends in Clinical Services Survey*, which is based on responses from 266 executives, was conducted through a combination of online and mail surveying. Sixty-five percent of the respondents were CEOs. More than half (56 percent) of respondents were from a standalone single hospital or facility, while 30 percent were from a single facility of a multihospital system. A large majority of respondents—79 percent—were from nonprofit hospitals.

**Selected survey results follow.
Read more analysis by attorneys Reggie Hill,
Thomas Bartrum and Bobby Guy
at www.wallerlaw.com.**

OUTSIDE ASSISTANCE

Hospital leaders weigh cost, culture and expertise when considering outsourcing arrangements.

Hiring an outside company to provide housekeeping, food services or supply chain assistance is nothing new for most hospitals. But a recent survey of hospital executives shows the outsourcing trend extends to clinical services as well—and most hospitals don't plan to stop anytime soon.

Seventy-eight percent of hospitals outsource at least one patient service, according to the *2006 Hospital Outsourcing Trends in Clinical Services Survey* sponsored by Waller Lansden Dortch & Davis, LLP. The survey of hospital CEOs and COOs found that 83 percent of respondents expect their facilities' outsourcing levels to stay the same or increase over the next two to three years.

Among the survey's other key findings:

- Fifty-five percent of respondents say vendor expertise is the primary reason for outsourcing.
- Dialysis services, sleep disorders and diagnostic imaging are the most outsourced patient services.
- The most common outsourcing arrangement (42 percent) is an agreement with an outside vendor in which the profits are retained by the hospital or system.

Hospital leaders say the outsourcing decision often comes down to two fundamental considerations: talent and cost. "It depends on whether the service they are providing is one they could provide at a greater economy of scale than we could provide in our own facility and still meet the high expectations of patient care," says Steve Hyde, COO of 320-staffed-bed Rio Grande Regional Hospital in McAllen, Texas.

When evaluating the availability

of talent, many hospitals—particularly those in rural areas—find that outside companies can pull from a wider base of professional staff.

"We are in a small area. It is very difficult to recruit to rural America, so it is easier to outsource and let somebody else do it for you," says Allan Zastrow, CEO of 100-staffed-bed Keokuk (Iowa) Area Hospital.

Finding a quality service provider for the right price is the most obvious hurdle for executives considering an outsourcing arrangement. But survey respondents also cite a significant cultural concern for many hospitals: losing control.

"The biggest hurdle is convincing your own organization that someone can bring the talent in and do it within your framework to meet your goals, especially if the organization has never done it before," says Michael McEachern,

COO of 338-licensed-bed Sisters of Charity Providence Hospital in Columbia, S.C.

Dennis Miller, CEO of 185-licensed-bed Williamson Medical Center in Franklin, Tenn., agrees. "You have to look at how it will fit into the culture of the institution," he says. "You have to be sure you still have control over any area you outsource."

Most hospital executives agree that clinical services outsourcing will remain a fact of life for the foreseeable future. Rio Grande's Hyde says organizations must continually re-evaluate outsourced services to determine whether such arrangements still make financial sense and meet patients' needs.

"Are we still getting good value for our money? Is it still what is best for patient care?" Hyde says. "We will always look at those, but it is not a foregone conclusion that we will do away with them."

SETTING THE COURSE FOR SUCCESSFUL OUTSOURCING

- Front-end planning, including regulatory and reimbursement planning, is critical.
- Good outsourcing decisions require coordination between multiple departments: administration, financial, risk management and legal.
- Liability risk and profitability risk are important—but often overlooked—considerations in the decision whether to outsource.
- Beware the false sense of security: Medical malpractice and regulatory problems of the outsourcer can impact the hospital, so insurance and indemnity are important.
- Recent price increases in insurance rates, and the prevalence of alternative insurance vehicles, have increased the risk that an outsourcing company's coverage could be inadequate; demand more than an insurance certificate (at a minimum, investigate the aggregate, know the insurer, become an additional insured, and require notice of material changes).
- Set clear standards, including performance and governance approval standards. A bad relationship can result in delayed and lost collections, lost admissions, ambulance diversions, morale issues, personnel turnover, lack of coordination in insurance plans, and reputational injury.
- Termination and unwind provisions are paramount to provide a clean exit; hospitals should preserve the right to terminate early and often.

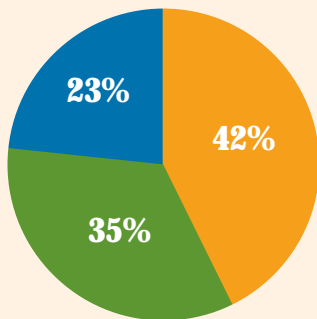
SURVEY RESULTS

2006 survey of hospital CEOs and COOs who are HealthLeaders subscribers.
Results based on 266 qualified responses. Margin of error: + /- 6.1%.

MODELS FOR OUTSOURCING ARRANGEMENT

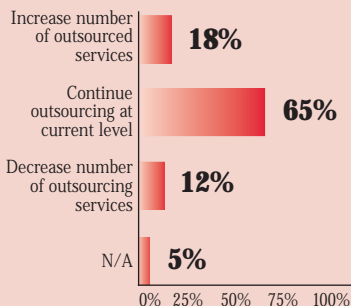
- Agreements with outside vendors, whereby the profits are retained by the hospital or system.
- Contractual arrangements, in which the manager retains the residual profits.
- Joint ventures, in which profits are split among the venture partners.

Percentage of all outsourced arrangements:



CHANGES IN OUTSOURCING

As you consider the next 2-3 years, is your hospital/system most likely to...



Why change outsourcing patterns?

The most frequently mentioned responses for increasing the number of outsourced services:

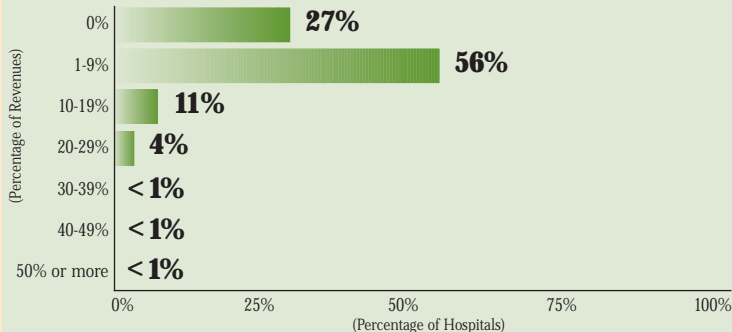
- Gaining access to capital; preserve internal capital
- Increase collaboration with physicians through JVs
- Expertise of vendors

The most frequently mentioned responses for decreasing the number of outsourced services:

- Costs of outsourcing too high; in-house more profitable
- Gain more control over the quality of the service

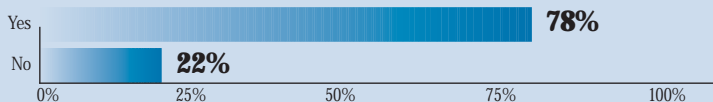
REVENUE FROM OUTSOURCING

What percentage of your hospital or system's total revenue is generated by outsourced patient services?

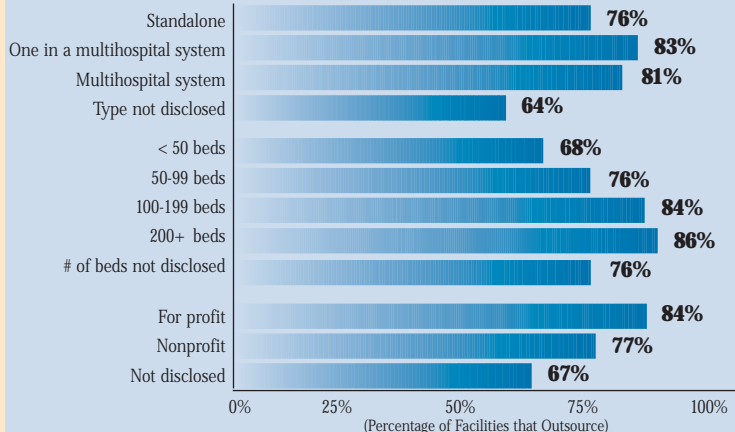


OUTSOURCING PATIENT SERVICES

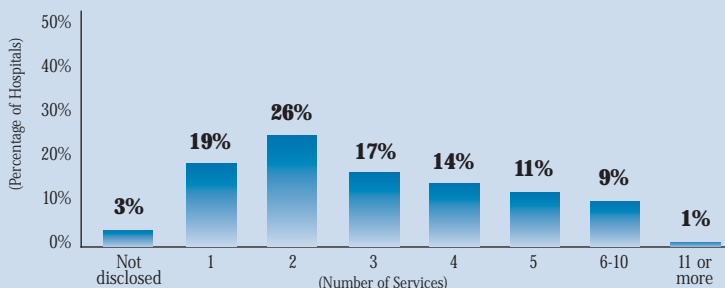
Does your organization outsource or contract for any patient services?



Breakdown of hospitals that outsource

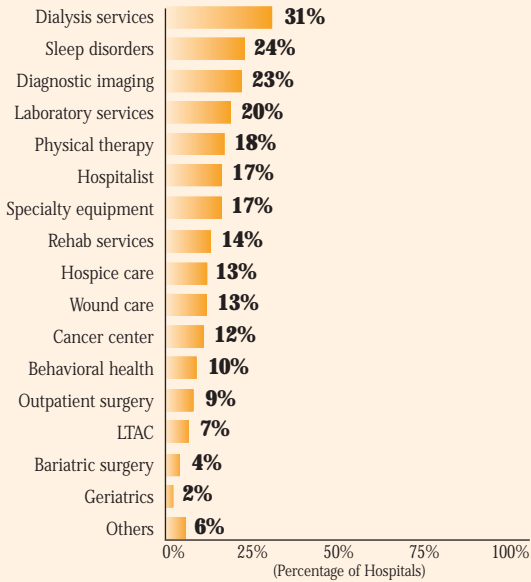


Number of clinical services outsourced

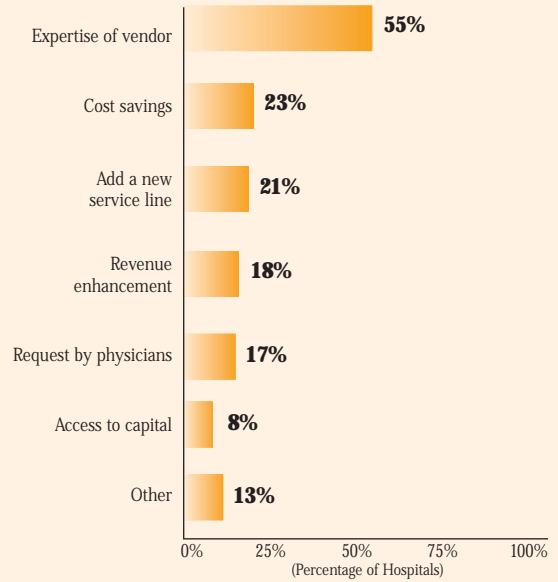


TYPES OF SERVICES

What types of services do you currently outsource?

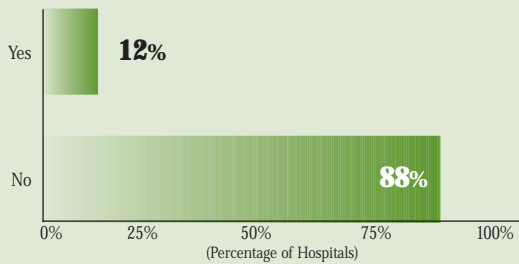


Why did you choose to outsource those services?

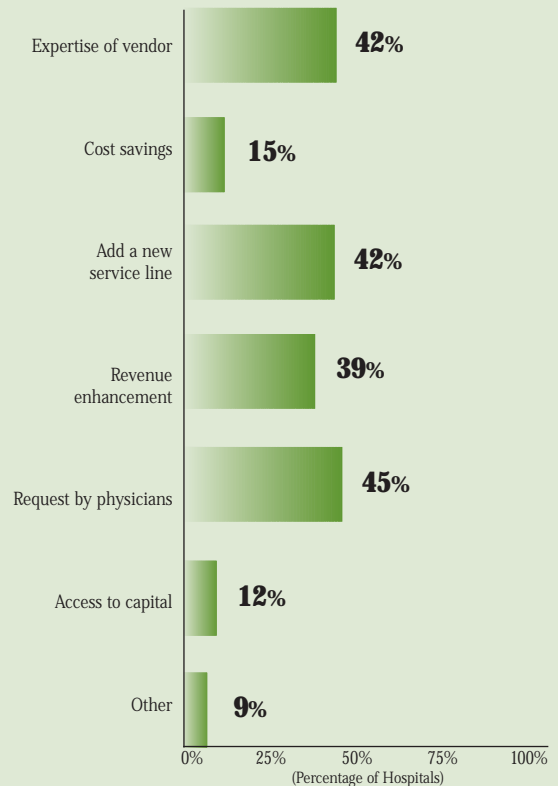


LOOKING AHEAD

Do you intend to outsource any additional patient services in the next 12 months?



If so, why will you outsource this service?



If so, what service?

