SEPTEMBER 2009

TECHNOLOGY

Gerard M. Nussbaum

hfm

healthcare financial management association www.hfma.org

healthcare financial management

assessing IT expenditures in an uncertain economy

One of the biggest challenges facing healthcare CFOs is knowing how to work with their CIOs to control IT costs while remaining responsible stewards of the organization's resources.

AT A GLANCE

Approaches that CFOs and CIOs may consider when determining how to gain the most value from IT investments at the least cost include:

> Portfolio review
> Contract review and negotiation
> Contract negotiation
> Analyses of IT spend, return, labor productivity, and strategic projects
> Lifecycle management
> Data management
> Taking advantage of crisis

A significant element of the economic stimulus bill is the investment in healthcare IT. The American Recovery and Reinvestment Act (ARRA) of 2009 offers significant incentives to both hospitals and individual providers to acquire and implement healthcare IT. However, the monetary incentives provided through the ARRA won't be enough to fully fund healthcare IT investments. These investments also will require significant capital from hospitals during a period of constrained funding. The potential for significant investment in healthcare IT through the economic stimulus bill does not make healthcare IT projects immune from the effects of the economic downturn: Many hospitals are planning to curtail capital projects, including IT and other technology projects, as part of their strategies for surviving the economic downturn (*Report on the Economic Crisis: Initial Impact on Hospitals*, American Hospital Association, November 2008).

IT cost cutting is not unique to health care. The economic downturn has immediate implications for CFOs, who are responsible for the economic viability of their hospital, and for IT executives, who must continue to support existing initiatives and deliver on new projects. In a recent survey, 42 percent of the businesses surveyed indicate that the priority for IT is cutting costs (Worthen, B., "Tech Executives Tighten Belts, Albeit Reluctantly," *The Wall Street Journal*, Dec. 16, 2008). Even in those institutions where cost cutting is not predominant, all departments, including IT, are facing flat budgets and/or are being requested to more carefully examine current spending. Controlling or cutting IT costs is not always straightforward, as many IT systems are critical to the operation of the enterprise. Furthermore, many costs are "baked into the cake" through multiyear maintenance and support contracts.

So how can CFOs work with CIOs to control healthcare IT costs and wisely undertake new IT projects that may be essential to achieving cost savings in other parts of the organization? CFOs and CIOs can lead healthcare organizations toward the pursuit of a multipronged approach to ensuring that the organization's IT expenditures are prudent.

Approaches to IT Cost Containment

There are several approaches CFOs and CIOs may consider when determining how to gain the most value from IT investments at the least cost.

Portfolio review. A portfolio review surveys all applications in use within the organization and identifies those that are substantially underutilized, are overlapping or duplicative, and/or are absent, resulting in direct operational inefficiency or the inability to collect significant monies. The portfolio review feeds into other approaches discussed below. The creation of a comprehensive list of applications, uses, and owners across the healthcare organization (not just under the control of the IT department) is helpful in prioritizing and understanding the organization's current IT spend. The portfolio review can also highlight situations where the organization has multiple applications that perform nearly identical functions, thus pinpointing opportunities for savings.

Contract review. A large portion of the average healthcare organization's annual nonpayroll IT budget is consumed by contractual commitments for maintenance and support services. Many IT departments do not have a good handle on the contracts for IT expenditures, the terms of these contracts, and the commitments involved. Gaining control over this portion of the IT spend requires a complete inventory of all contracts for technology (note: not just IT). This is a task that should be undertaken in consultation with the hospital purchasing and legal departments. The goal is to arrive at a comprehensive inventory of the contracts in place, assess renewal/cancellation deadlines, identify opportunities for leveraging savings, and assess current usage levels against licensing (too high/too low). Combined with the portfolio review, this initiative will support contract renegotiation efforts.

Contract renegotiation. An important goal of contract renegotiation is to seek reduced pricing from vendors and lengthened payment periods to achieve cash flow savings. This goal can be achieved by:

- Creating competition between vendors to reduce costs while eliminating duplicative or overlapping applications, based upon the portfolio review
- Determining whether lengthening contract terms can lead to immediate costs savings
- More strenuously enforcing contract clauses to improve vendor performance or extract other concessions

A review of IT inventory and a first-pass summarization of contract terms could be performed by a knowledgeable senior buyer or a senior IT analyst with an understanding of broader business issues. Subsequent review by IT senior management should be undertaken to identify and prioritize the opportunities for renegotiation. At the outset, contract renegotiation is a business-driven process; hospital counsel should be involved in the revision of any contractual terms, but should not be the driver of the renegotiation process, as it is better to have an experienced healthcare information systems negotiator in charge of this effort.

Spend analysis. The assigned IT analyst should work with accounting and purchasing personnel to create a full accounting of technology-related spending. This analysis, across all departments, should be used to identify duplicative service purchases, opportunities for vendor consolidation, potential leverage for lower costs, and services that should be brought in house, as well as to highlight contracts missed in the contract and portfolio analysis. This analysis should also be used as an input to a sensitivity analysis to assess the impact of certain cutbacks, if necessary.

Return analysis. In recent years, IT projects have been subjected to more rigorous return analysis. Now, when money is becoming tighter, linking IT projects to clear corporate objectives and return (whether monetary or value-driven) is increasingly important. Reviewing original project goals, identifying measurable outcomes to be achieved, and successfully achieving those outcomes are elements of driving value from existing and proposed IT solutions.

Labor productivity analysis. Examining the work performed by the IT staff, use of contractors, and the amount of time spent by IT staff on projects provides a basis for identifying labor productivity opportunities. The goal here is not so much about reducing headcount as it is redeploying resources to work that is of higher value to the organization.

Even in this time of rising unemployment, certain highly skilled resources remain in short supply. Thus, it is imperative to ensure that the organization is applying the talents of its technology professionals to projects of highest value, especially before undertaking new projects. To this end, labor productivity analysis should actively seek out ways to eliminate low-value work, push it down to less costly resources, or automate the task.

Strategic project analysis. All IT projects should be examined using a consistent prioritization approach. Just as the return analysis should focus on the value delivered to the organization, the strategic project analysis should focus the IT resources on a smaller set of projects with the goal of obtaining design benefits sooner. Thus, rather than focusing IT department resources on 20 projects that will ultimately deliver value in two to three years, the IT department could complete eight projects within six to nine months and obtain the benefits of these projects when they are most needed. The strategic project analysis could also refocus priorities on smaller projects with more rapid benefits delivery.

Lifecycle management. Older systems often have disproportionately high costs due to use past the warranty term, high maintenance costs, and the need to retain inefficient legacy hardware and software. The goal in analyzing all data center and other equipment is to determine whether a more active retirement approach will lower net costs. Many hospitals retain nonproduction legacy systems solely because the department cannot let go of the security blanket. In instances in which the data within these nonproduction systems need to be retained, offline retention methods (e.g., enterprise report management [ERM], imaging of reports) or conversion of the data to a structured query language database with query tools may be more cost effective. Maintenance costs will decrease, data space can be freed, and electricity and operating costs may also be reduced.

A lifecycle analysis can also be used as an input to a finance-driven process of capital allocation and cash flow planning. This analysis can also feed a process to reassess the use of leasing and other financing techniques to fund necessary IT acquisitions when capital funding is tight.

Data management. Looking at *how* data are managed across the organization—whether on core IT-managed systems or in departmental areas—offers opportunities to reduce expenditures. Such analyses often reveal areas of substantial data duplication and retention of outdated data. Furthermore, healthcare organizations often retain less-critical data on expensive data storage levels. These efforts can be concomitant with the need to manage data to achieve compliance with legal data retention policies and provide a push to the organization to dispose of data. This presents an opportunity for a healthcare organization to examine data management policies and their enforcement, moving toward an enterprise data management model that leverages technology to reduce the growth of storage and the effort required to manage the data while improving compliance with security and privacy laws.

Readiness to respond to a crisis. Hospitals with robust balance sheets may also be able to take advantage of the economic turmoil to snap up IT assets, especially those that improve operational redundancy, from other businesses that are forced to close or sell off assets.

Sound Strategies in a Struggling Economy

Actions of the type discussed above should help hospitals emerge from the recession stronger, more efficient, and in a better position to meet the demands of delivering technology to support the delivery of health care. Many of these activities may also be applied in other hospital areas to enable the executive team to use a consistent method to identify savings and focus the hospital's resource use on efforts of maximum benefit to its long-term health, as well as to address shorter-term budgetary and cash flow issues.

Clearly, all hospital departments will need to change due to the economic factors sweeping the nation. Regardless of the effects of the federal economic stimulus efforts, cutbacks and cost savings will still be needed. The CFO, CIO, and all members of hospital senior management face an important choice: They can either approach the economic situation reactively, or they can begin today to take proactive steps to better manage the use of available resources and thereby emerge from the current economic situation in a stronger position and with a greater ability to serve the health needs of their communities. ●

Gerard M. Nussbaum, JD, CPA, is director of technology services, Kurt Salmon Associates, New York (gerard.nussbaum@kurtsalmon.com).

Atlanta	Minneapolis	New York	San Francisco Bay Area
404.892.3436	612.378.1700	212.319.9450	650.616.7200