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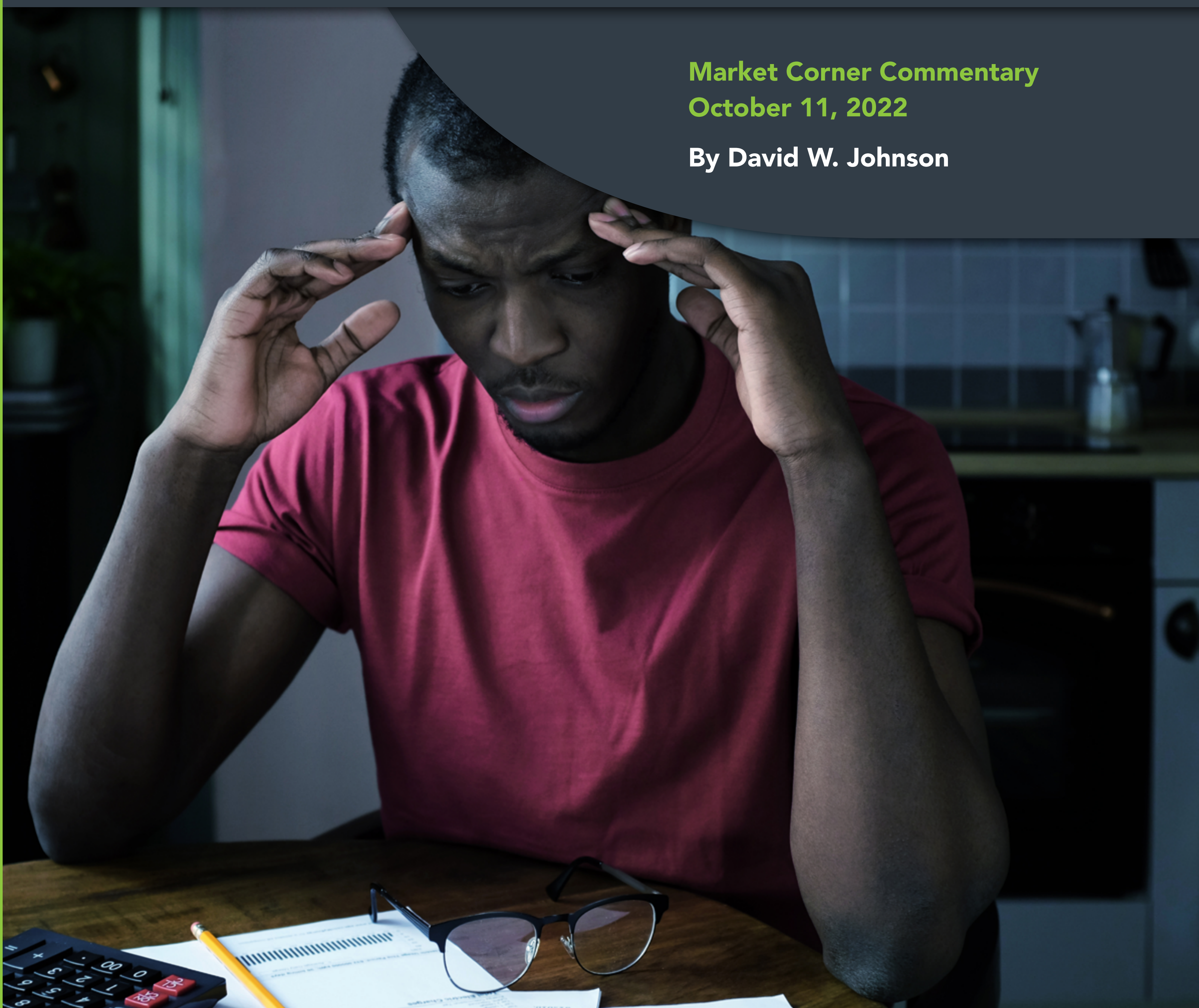
In Defense of Value:
A Response to Ken Kaufman



Market Corner Commentary
October 11, 2022

By David W. Johnson

In an Oct. 5, 2022, commentary, Ken Kaufman offers a full-throated and heartfelt defense of non-profit healthcare during a time of significant financial hardship. Ken describes 2022 as "the worst financial year for hospitals in memory." His concern is legitimate. The foundations of the nonprofit healthcare business model appear to be collapsing.

I've known and worked with Ken Kaufman for decades. He is the life force behind Kaufman Hall, a premier financial and strategic advisor to nonprofit hospitals and health systems. The American Hospital Association uses Kaufman Hall's analysis of hospitals' underlying financial trends to support its plea for more federal funding.

Beyond the red ink, Ken laments the "media free-for-all challenging the tax-exempt status, financial practices, and ostensible market power of not-for-profit hospitals and health systems." He is referring to three recent investigative reports on nonprofits' skimpy levels of charity care (*Wall Street Journal*), aggressive collection tactics (*New York Times*) and 340B drug purchasing program abuses (*New York Times*).

Ken has never been timid about expressing his opinions. He's passionate, partisan and proud. His defense of nonprofit healthcare chronicles their selfless care of critically ill patients, the 24/7 demands on their resources and their commitment to treating the uninsured. These "must have clinical services… don't just magically appear." Nonprofit healthcare needs "our support and validation in the face of extreme economic conditions and organizational headwinds."

Given his personality, it's not surprising that Ken's strident rhetoric in defending nonprofit healthcare mimics the famous "You can't handle the truth" exchange between Lieutenant Kaffee (Tom Cruise) and Colonel Jessup (Jack Nicholson) from the 1992 movie "A Few Good Men." Kaffee presses Jessup on whether he ordered a "code red" that led to the death of a soldier under his command. When Kaffee declares he's entitled to the truth, Jessup erupts,

> ***… I have neither the time nor the inclination to explain myself to a man who rises and sleeps under the blanket of the very freedom I provide and then questions the manner in which I provide it. I would rather you say, "thank you" and be on your way.***

Should American society just say "thank you" to nonprofit healthcare and fork over the massive incremental funding required to sustain current operations?

TRUTH AND CONSEQUENCES

The social theorist Thomas Sowell astutely observed, "If you want to help someone, tell them the truth. If you want to help yourself, tell them what they want to hear." In his commentary, Ken Kaufman is telling nonprofit healthcare exactly what they want to hear. The truth is more nuanced, troubling and inconvenient.

Healthcare now consumes 20 percent of the national economy and the American people are sicker than ever. Despite the high healthcare funding levels, the CDC recently reported in U.S. life expectancy dropped almost a full year in 2021. Other wealthy nations experienced increases in life expectancy. Combining 2020 and 2021, the 2.7-year drop in U.S. life expectancy is the largest since the early 1920s.

During an interview regarding the September 28, 2022, White House Conference on Hunger, Nutrition and Health, Senator Cory Booker highlighted two facts that capture America's healthcare dilemma:

- One in three government dollars funds healthcare expenditure; and
- Half of Americans suffer from diabetes or pre-diabetes.

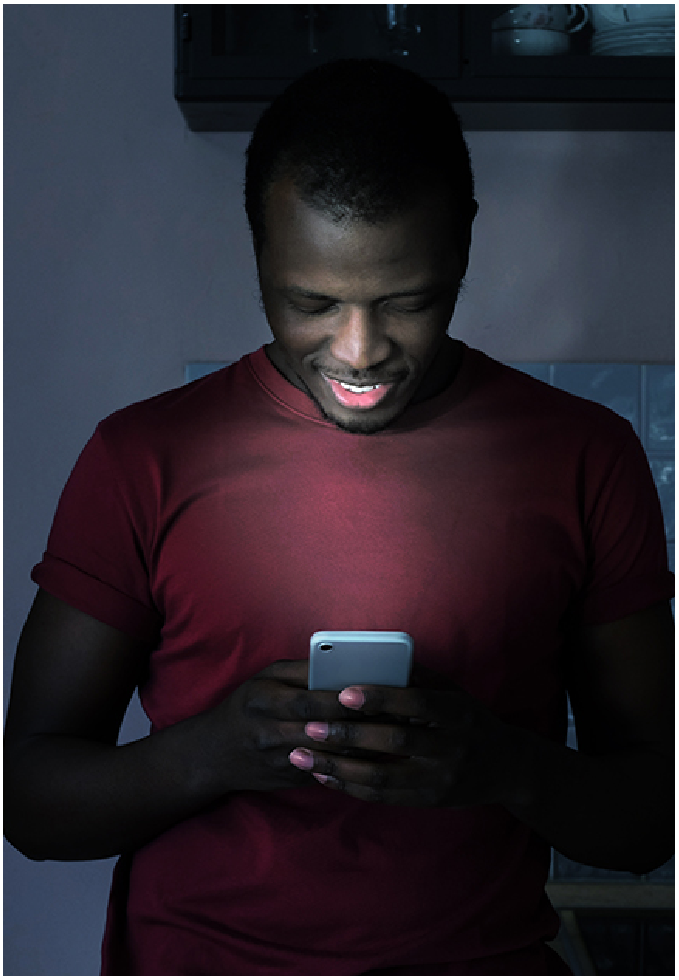
As a nation, we're chasing our tail by prioritizing treatment over prevention. Particularly in low-income rural and urban communities, there is a breathtaking lack of vital primary care, disease management and mental health services.

Instead of preventing disease, our healthcare system has become adept at keeping sick people alive with a diminished life quality. There is plenty of money in the system to amputate a foot but little to manage the diabetes that necessitates the amputation.

Despite mission statements to the contrary, nonprofit healthcare follows the money. The only meaningful difference between nonprofit and for-profit healthcare is tax status. Each seeks to maximize treatment revenues by manipulating complex payment formularies and using market leverage to negotiate higher commercial payment rates.

According to Grand View Research, the market for revenue cycle management in 2022 is $140.4 billion and forecasted to grow at a 10.3% annual rate through 2030. By contrast, Ibis World forecasts the U.S. automobile market to grow 2.6% in 2022 to reach $100.9 billion. Unbelievably, in today's America, processing medical claims is far more lucrative than manufacturing and selling cars and trucks.

According to CMS's National Expenditure Report for 2020, hospitals (31%) and physicians and clinical services (20%) accounted for over half of national healthcare expenditures. This included $175 billion allocated to providers through the CARES Act. Despite the massive waste embedded within healthcare delivery, the CARES Act monies gave providers



the illusion that America would continue to fund its profligate and often ineffective operations.

It's not at all surprising that healthcare providers now want, even expect, more emergency funding. Change is hard. Not even during COVID did providers give up their insistence on volume-based payment. Providers did not embrace proven virtual care and hospital-at-home business practices until CMS guaranteed equivalent payment to existing in-hospital/clinic service provision.

Even with parity payment and the massive CARES Act funding, there was uneven care access for COVID patients. Particularly in low-income communities, tens of thousands died because they did not receive appropriate care.

More of the same approach to healthcare delivery will yield more of the same dismal results. Healthcare providers have had over a decade to advance value-based care (VBC). VBC provides the right care at the right time in the right place at the right price. There's far too little.

Instead of pursuing VBC, providers have doubled-down on volume-driven business models that attract higher-paying commercially-insured patients. Despite the relative ease of migrating service provision to lower-cost settings, providers insist on operating high-cost, centralized delivery models (think hospitals). They want society, writ large, to continue paying premium prices for routine care.

It's time to stop. As a country, we need less healthcare and more health.

A FOURTH QUESTION

When I give speeches to healthcare audiences, I typically begin with three yes-or-no questions about U.S. healthcare to establish the foundation for my subsequent observations. Here they are:

- Question #1: The U.S. spends 20% of its economy on healthcare. The big country with the next highest percentage spend is France at 12%. How many believe we need to spend more than 20% of our economy to provide great healthcare to everyone in the country? No one ever raises their hand.

- Question #2: The CDC estimates that 90% of healthcare expenditure goes to treat individuals with chronic disease and mental health conditions. How many believe we are winning the war against chronic disease and mental health conditions? No one ever raises their hand.

- Question #3: Given the answer to the previous two questions, how many believe the system needs to shift resources from acute and specialty care into health promotion, primary care, chronic disease management and behavioral health? Everyone raises their hand.

This short exercise is quite revealing. It demonstrates that healthcare doesn't have a funding problem. It has a distribution problem. It also demonstrates that providers aren't adequately addressing our most critical healthcare challenge, exploding chronic disease and mental health conditions. Finally, it shows that the healthcare system needs major restructuring.

The real questions about reforming healthcare are less about what to reform and more about how to undertake reform. The increasing media scrutiny that Ken Kaufman references as well as growing consumer frustrations with healthcare service provision, demonstrate that healthcare is losing the battle for America's hearts and minds.

Markets are unforgiving. The operating losses most nonprofit providers are experiencing reflect a harsh reality. Their current business models are not sustainable.

An economic reckoning is underway. The long arc of economics points toward value. As healthcare deconstructs, the nation's acute care footprint will shrink, hospitals will close and value-based care delivery will advance. The process will be messy.

The devolving healthcare marketplace led me to ask a fourth question recently in Nashville during a keynote speech to the Council of Pharmacy Executives and Suppliers. Here it is:

- Question #4: As the healthcare system reforms, will that process be evolutionary (reflecting incremental change) or revolutionary (reflecting fundamental change)? Two-thirds voted that the change would be revolutionary.

That response is just one data point but it reflects why post-COVID healthcare reform is different than previous reform efforts. The costs of maintaining status quo healthcare are simply too high. From a policy perspective, either market-driven healthcare reforms will drive better outcomes at lower costs (that's my hope) or America will shift to a government-managed healthcare system like those in Germany, France and Japan.

Like Ken Kaufman, I admire frontline healthcare workers and believe we need to make their vital work less burdensome. I also sympathize with health system executives who are struggling to overcome legacy business practices and massive operating deficits. Unfortunately, most are relying on revenue-maximizing playbooks rather than reconfiguring their operations to advance consumerism and value-based care delivery.

Unlike Ken Kaufman, I believe it's time for some tough love with nonprofit healthcare providers. Payers must tie new incremental funding to concrete movement into value-based care delivery. This was the argument Zeke Emanuel, Merrill Goozner and I made in a two-part commentary (part 1; part 2) in Health Affairs earlier this year. It's also why the HFMA, where I serve on the Board, has made "cost effectiveness of health (CEoH)" its new operating mantra.

While this truth may be hard, it also is liberating. Freeing nonprofit organizations from their attachment to perverse payment incentives can create the necessary impetus for embracing consumerism and value. Kinder, smarter and affordable care for all Americans will follow.

AUTHOR

David Johnson is the CEO of 4sight Health, a thought leadership and advisory company working at the intersection of strategy, economics, innovation and capital formation. Dave wakes up every morning trying to fix America's broken healthcare system. Prior to founding 4sight Health in 2014, Dave had a long and successful career in healthcare investment banking. He is a graduate of Colgate University and earned a Masters in Public Policy from Harvard Kennedy School. Employing his knowledge and experience in health policy, economics, statistics, behavioral finance, disruptive innovation, organizational change and complexity theory, Dave writes and speaks on pro-market healthcare reform. His first book ***Market vs. Medicine: America's Epic Fight for Better, Affordable Healthcare***, and his second book, ***The Customer Revolution in Healthcare: Delivering Kinder, Smarter, Affordable Care for All*** (McGraw-Hill 2019), are available for purchase on www.4sighthealth.com. His third book, ***Less Healthcare, More Health: The Prescription for a Happier, More Equitable and Productive America***, will publish in 2024.