The Scale Imperative for Academic Medical Centers: Part 1—Approach

Alan M. Zuckerman, FACHE, FAAHC, president, Health Strategies & Solutions, Philadelphia, Pennsylvania, and Robert N. Golden, MD, Robert Turell professor in medical leadership, dean of the School of Medicine and Public Health, and vice chancellor for medical affairs, University of Wisconsin–Madison

The rapidly changing healthcare environment is driving strategic reshuffling and competitive responses that will permanently alter the operational landscape for all healthcare organizations. Community-based healthcare providers across the country in particular are rapidly moving to large, vertically integrated healthcare systems. As these organizations grow and develop, they are becoming closed systems of care and developing tertiary and quaternary care capabilities. In addition, these providers are reducing, and eventually eliminating all but a trickle of, the flow of specialized referrals to academic medical centers (AMCs). At the same time, the focus of available research funding is shifting from basic research toward clinical, translational, population health, and comparative effectiveness platforms. These reductions in funding and the loss of referrals threaten the sustainability of AMCs' research and teaching missions.

SUCCEEDING IN THE NEW ENVIRONMENT

In our work with AMCs, we have identified five strategic imperatives for their success in the healthcare delivery landscape of the future:

1. *Sufficient scale and scope:* Organizations must scale up or focus to survive in the future. For most, scaling up will involve inorganic growth through mergers, acquisitions, and new partnerships. In major metropolitan areas, a limited number of consolidated organizations will emerge, probably with annual revenues in excess of $2 billion.
2. *Cost competitive:* Being cost competitive has never mattered before, but with the new underlying financial pressures emerging, all organizations will need to continually reduce costs for the foreseeable future, by about 3–5% annually. Competition for patients will also increasingly be based on ability to provide value (quality + service ÷ cost).
3. *Demonstrated quality:* Quality is part of the value challenge and is increasingly important considering the impact of pay-for-value reimbursement from the federal government and the initiation of quality incentive–based contracts by

certain payers. As quality measurement improves, the reimbursement focus will shift toward outcomes and away from the current structure and process measures.

4. *Exceptional service:* Also part of the value challenge, a focus on exceptional service has caused nearly all organizations to materially raise their game over the past 10 years. Since healthcare is fundamentally a service business, rigor in this area will continue to be a key aspect of competitive success in the future.
5. *Real integration:* Success with the last three challenges, in particular, will necessitate not just having all the players or parts of a system of care, but knitting them together in a truly integrated manner across the continuum.

While some AMCs have moved rapidly to build scale, many others have not, and AMCs as a whole have been slower than their community-based and for-profit competitors to scale up (Peterson, 2014). Thus, of the five strategic imperatives, we limit our discussion to the first imperative for AMCs, scale and scope.

What Level of Scale Do AMCs Require?

From a market conditions/dynamics perspective, the most important factor in determining scale is the current and likely future degree of provider consolidation in the market. A highly consolidated market may disadvantage independent organizations, while a fragmented market should not. In terms of the population base required, smaller and less highly developed AMCs usually need a population of 1 to 2 million persons, and larger, more highly developed centers require upwards of 3 million persons to support some of their subspecialized capabilities (Finarelli, 2009). Many pediatric subspecialties, as well as areas such as transplantation and burn care, require very large populations to support the financial and clinical viability of services.

As the market consolidates and organizes into increasingly closed systems of care, unique services, carve-outs, and ad hoc informal referrals for tertiary and quaternary care will become far less prevalent. For a market that is, on average, 50% consolidated and moving toward organized systems of care, the "free agent" population required to support subspecialized programs is roughly twice as large as the population base cited above. At 75% consolidation and systematization, the population base needed is about four times as large (AthenaHealth & Halley Consulting, 2012).

AMCs' Approaches to Scale

Current AMC approaches to scale can be described using a five-category framework.

1. *Large-scale consolidators.* A small number of AMCs have moved aggressively to build scale on an extraregional and, often, national and international level. For example, Duke Medicine, in addition to its growing network in North and South Carolina, has partnered with LifePoint to accelerate its growth in and beyond the Carolinas.

2. *Regional integrators.* A larger, but still relatively small, number of AMCs have focused their scale strategy primarily or exclusively within the region they have historically served. One example of this approach is UMass Memorial Health Care in central Massachusetts scaling up in this area.

3. *Proactive collaborators.* A few AMCs have adopted an innovative partnering approach to scale development in which university- and community-based organizations band together to build scale. A notable example is a joint venture of University of Colorado Hospital and Poudre Valley Health System.

4. *System members.* A small number of university hospitals have decided to become (minority) members of larger healthcare systems. More often than not, financial difficulties experienced by the university hospital forced this move. A recent example of this model is Loyola University Health System joining Trinity Health System.

5. *Independents.* Though no AMC is truly and completely independent, many retain a mostly independent status. In some cases, large systems have developed in the AMC's region, thus effectively precluding an AMC's system development options other than system membership, or possibly proactive collaboration, while in other cases these AMCs appear to be pursuing the traditional strategies of largely organic growth and clinical and academic affiliations. University of Chicago Medicine is an example of this approach.

Part 2 of this column, to be published in the March/April 2015 issue of *JHM*, features a case study to demonstrate the application of these approaches.

The resistance of AMCs to the broader industry evolution is driven by three main factors: Many are still performing well enough financially; the core academic entity is concerned about dilution of and diversion from its mission in a larger, clinically oriented enterprise; and the cultural divide between academic- and community-based providers is difficult to bridge.

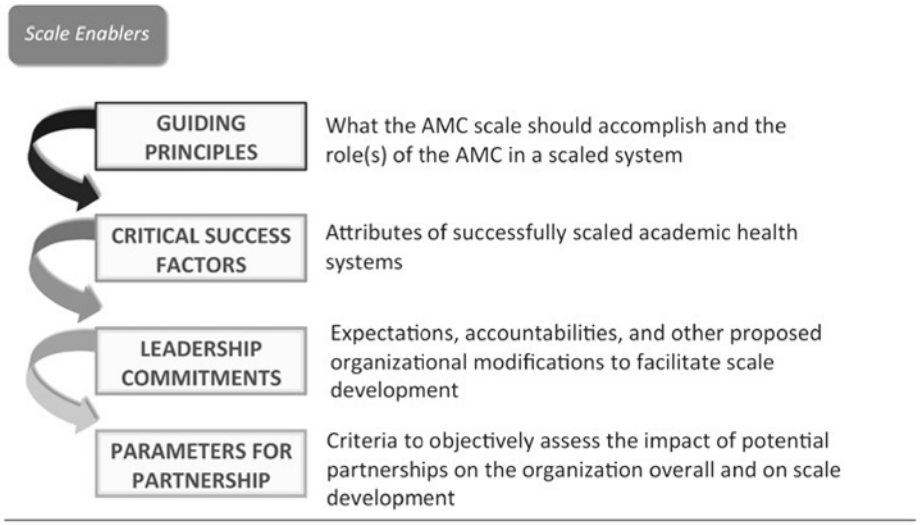
ENABLERS OF SCALE DEVELOPMENT

Some AMCs reached the decision to scale up but were unsuccessful in doing so. While market conditions and dynamics can play a role in foiling this strategy, internal politics and decision making often disable strategy implementation. The successful execution of a scale strategy requires internal clarity and an integrated approach. Figure 1 presents a framework for enabling scale development, and each element is described in this section.

Guiding Principles

First, leaders need to have crisp, relevant answers to the question, Why we are doing this? Outcomes should relate to the core academic mission of the AMC, its market relevance, and its financial viability. Each AMC will drive toward its own necessary outcomes, as illustrated in the following example from one AMC.

FIGURE 1
Enabling Scale Development: Principles, Success Factors, Commitments, and Parameters



A framework to enable and manage the AMC's scale imperative

This AMC divided its outcomes framework into two segments: what scale should be achieved, and what the AMC's role should be in scale development.

Sample AMC's Principles Dictating What Scale Should Be Achieved

- Materially contribute to market relevance and support academics.
- Materially contribute to financial viability and support academics.
- Enhance position in high-end tertiary/quaternary care for
  - teaching/research/national standing;
  - faculty recruitment and retention; and
  - financial reasons, especially in transition to the new era.
- Advance the mission of public health and the role as a public institution by
  - providing or advancing a new model of care for learners and
  - materially contributing to the health status and serving public need for the state and beyond.

The third and fourth principles in the above list are particularly relevant to fulfilling the scale imperative.

Sample AMC's Principles for Determining Its Role in Scale Development

- Be a leader in a new delivery system.
- Provide access, directly and indirectly, to all healthcare services that are needed by the local/regional population.
- Undertake multiple and concurrent paths to secure populations.

- Prioritize scaling efforts and investments by level of risk and the opportunity it presents by
  - establishing and following formal parameters to facilitate strategic partnerships in furtherance of scale.

One role the AMC will not play in scaling up is owning, or even fully controlling, all parts of the care continuum.

The guiding principles also define the role that the AMC will play and set important ground rules in establishing a scaled system and the scope of services desired. Importantly, as shown in the above example, the principles can help identify what the AMC will not do in scaling up.

Critical Success Factors

As discussed previously, internal factors, not desire to execute the scale strategy, often constrain the AMC's ability to move forward with system growth. AMCs that have successfully executed a scale strategy typically have the following organizational culture and orientation characteristics:

- They function in an integrated or unified manner across the organization.
- They are at least somewhat risk bearing.
- They view their future as much broader than being just a referral center for the extended service area and have aligned internal and external incentives to support delivering high-value care with a population health orientation and as active leaders of accountable care.
- They increasingly view their customers as value-based buyers of care.
- They are decisive and adapt well to change.

Many of these qualities are at odds with the traditional AMC culture. Creating a new culture in a large organization like an AMC is no easy task. Successful culture change requires imaginative and visionary leaders and a great deal of hard work. Part 2 of this column will feature the case study of an AMC that has taken on this challenge.

Leadership Commitments

To advance a new organizational culture, a different set of leadership capabilities and commitments will be needed. If leadership is not fully committed to cohesion, collaboration, and building scale, including tackling the often difficult intraorganizational issues, internal forces will block growth. Part 2 of this article discusses leadership commitment in more detail in the context of the case study.

Parameters for Assessing Partnership Potential

As the AMC goes out to the market to begin the task of scaling up, many varied and complex opportunities will arise for growth. To determine which opportunities should be accorded high priority, a set of criteria (consistent with the guiding

principles selected by the organization) by which to evaluate the opportunities is critical. At a minimum, the criteria allow a reasonably objective assessment of each opportunity and, when multiple opportunities present at the same time, afford the ability to rank the concurrent possibilities.

The following parameters help an AMC assess a partnership's potential for success:

1. Is it a high-priority risk or a submarket opportunity?
   a. What is the opportunity cost of pursuing this partnership?
   b. How much risk does it create relative to existing relationships?
2. To what degree will it increase the following?
   a. Overall base of population served
   b. Breadth and depth of the care continuum
   c. Quaternary volume in key programs
3. What "tentacles" does it create for the AMC in the market?
   a. What relationships are possible with hospitals or systems, payers, physicians, and employers?
4. What amount of capital investment will be required?
5. What is the range of expected return on investment, and by when?
6. How significantly will it affect the following?
   a. Achievement in the academic missions
   b. Each of the AMC's entities
   c. The AMC's scale development overall

CONCLUSION

All healthcare systems will need to consider the advantages of scale as they confront the evolution of reform and changes in reimbursement models. For AMCs, the scale imperative is even greater, not only for the future viability of their clinical mission but also to secure the vitality of their academic mission.

REFERENCES

AthenaHealth & Halley Consulting Group. (2012, October). ReferralView: A first look at national referral patterns from primary care practices. Retrieved from http://www.athenahealth.com/_doc/pdf/whitepapers/ReferralView_2012.pdf

Finarelli, H. J. (2009). *The hospital executive's guide to physician staffing* (pp. 87–88). Marblehead, MA: HCPro,

Peterson, H. (2014, January 7). Challenging healthcare landscape fertile ground for AMC repositioning. *Becker's Hospital Review*. Retrieved from http://www.beckershospitalreview.com/strategic-planning/challenging-healthcare-landscape-fertile-ground-for-amc-repositioning.html

For more information about the concepts in this columns, contact Mr. Zuckerman at AZuckerman@hss-inc.com.

The Scale Imperative for Academic Medical Centers: Part 2—Case Study

Alan M. Zuckerman, FACHE, FAAHC, president, Health Strategies & Solutions, Philadelphia, Pennsylvania, and Robert N. Golden, MD, Robert Turell professor in medical leadership, dean of the School of Medicine and Public Health, and vice chancellor for medical affairs, University of Wisconsin–Madison

In our previous column in this series (see the Operations and Strategy column in the January/February 2015 issue of *JHM*), we describe the scale imperative for academic medical centers (AMCs) if they wish to remain viable in a healthcare landscape characterized by consolidation, increasingly closed systems, new reimbursement models, decreased funding, and other challenges. In addition, we describe AMCs' approaches to achieving adequate scale in terms of our five-category framework. The framework, with additional examples, is revisited in the sidebar on page 87 of this issue.

Here, we discuss the case of one AMC—UW Health—that has embarked on the journey to developing scale. It hopes to leverage scale in shoring up its ability to support its missions of research and education.

ABOUT UW HEALTH

UW Health is the umbrella organization for the clinical operations of the various University of Wisconsin–Madison entities—UW School of Medicine and Public Health, UW Medical Foundation (the academic group practice), and UW Hospital and Clinics (the academic teaching hospital). Located in Madison, Wisconsin, a relatively small market in south central Wisconsin, UW Health's clinical mission involves providing service locally, regionally, statewide, and across state lines into the adjacent states of Illinois and Iowa. UW Health has had excellent financial performance for the past 15 years and remains strong today. UW School of Medicine and Public Health's academic performance and reputation also have been consistently strong throughout this period.

THE DECISION TO SCALE UP

In addition to the national trends affecting all AMCs, UW Health faced a number of external conditions that influenced its decision to scale up:

- It is surrounded by five large regional/national systems—Mayo Clinic, Ministry Health Care/Ascension Health, Aurora Health Care, Advocate Health Care, and UnityPoint Health—that have been growing rapidly and moving toward

Five-Category Framework for Approaches to Scaling Up

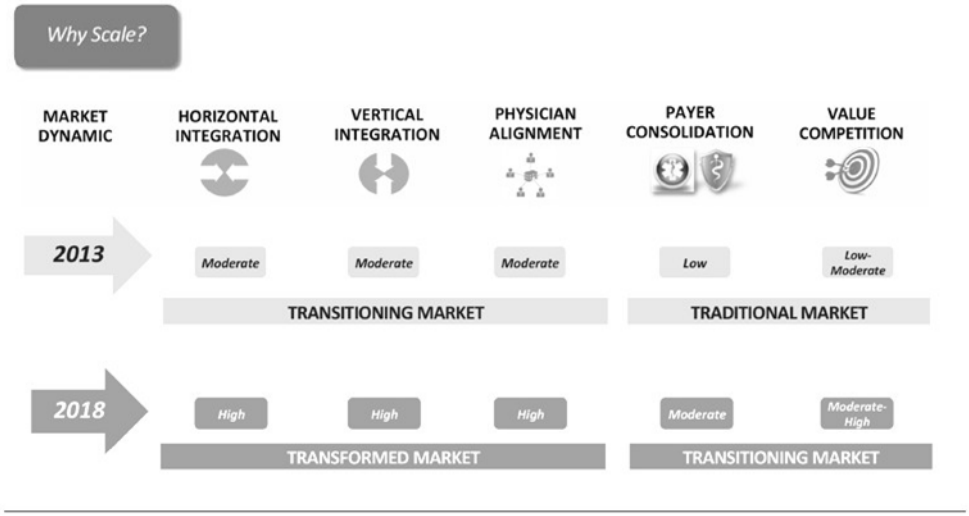
1. *Large-scale consolidators.* The University of Pittsburgh Medical Center continues to expand its network throughout western Pennsylvania. It also owns and operates a hospital in Ireland and a number of other international ventures. Cleveland Clinic has a large network in northeast Ohio; a presence in Florida and Nevada; national contracts with Lowes, Walmart, and others; a new joint venture with Community Health Systems; and international ventures in Canada and Abu Dhabi.
2. *Regional integrators.* UMass Memorial Health Care in central Massachusetts, and University of California Los Angeles Health System in west Los Angeles.
3. *Proactive collaborations.* Indiana University Health (formerly Clarian Health), a joint venture of Indiana University Hospital and Methodist Hospital; and Lifespan, which was founded by Rhode Island Hospital (the major teaching hospital for the Warren Alpert Medical School of Brown University) and The Miriam Hospital.
4. *System members.* Creighton University Medical Center joined Alegent Health.
5. *Independents.* University of Chicago Medicine is growing organically through new or expanded programs.

Madison from all directions. In early 2014, UnityPoint Health completed its acquisition of Meriter Health in Madison and established a local presence, while the formerly independent Dean Clinic sold itself to SSM Health Care, based in St. Louis, Missouri.

- The relatively high cost of healthcare in the Madison region is not likely to be sustainable.
- About 60% of the quaternary referrals to UW Health, which yield very high contribution margins, are outside its control and at risk as surrounding systems grow and become increasingly self-contained.

As UW Health looks into the future, it expects to encounter daunting clinical challenges, as noted in Figure 1. Although its market in 2014 was moderately integrated both horizontally and vertically (including physician alignment), payers are still many, and diverse, and competition on value is modest. Over the next 5 years, the market is expected to evolve across all five of these factors. The result is that UW Health faces a transforming market that is likely to move quickly toward highly organized and increasingly closed systems of care, thus placing at risk the tertiary and quaternary referrals from throughout the state that have been the lifeblood of its clinical growth and academic support.

FIGURE 1
Key Implications for the Wisconsin Market: Today and Tomorrow



Consensus among leaders is that the Wisconsin market will continue to transition and be closer to transformed by 2018

UW HEALTH'S APPROACH

In response to these challenges, UW Health set about creating a culture that will support the scale imperative by identifying the leadership commitment and degree of scale required.

Leadership Commitments

To advance a new organizational culture, a different set of leadership capabilities and commitments is required. These competencies are quite different from the leadership expectations in most AMCs. If leadership is not fully committed to cohesion, collaboration, and building scale, including tackling the often difficult intraorganizational issues, internal forces will block growth. Scaling up requires support staff to fuel inorganic growth and then a new support structure to manage a larger, more diverse, and geographically dispersed organization. The following illustrates the types of leadership commitments needed for growth:

- Ensure that the AMC functions as one organization (including all clinical departments)
- Set expectations that departments/chairs and administration will work together
- Streamline the decision-making process
- Establish a dedicated infrastructure to support the above

- Formally determine:
  - the menu of options available to achieve the scale required
  - how the various AMC entities can balance risk and reward and not be adversely affected by scaling strategies and partnership arrangements
  - mitigation strategies for political, economic, and other risks

Level of Scale

UW Health's leaders approached the issue of required scale with two questions: How can UW Health access the population to support subspecialized programs and capabilities, and what scale will be required to remain competitive within the context of evolving local, regional, and statewide market conditions?

UW Health determined that the population required to support quaternary services today ranges between 2,400,000 and 2,800,000 persons; by 2018, it will increase to 3,700,000 to 5,600,000 persons (unpublished report, "UW Market Focus: Scale and Strategic Perspectives," May 2013). The major causes of the growth needed in the size of the population base are twofold: increasingly subspecialized programs under development by UW Health, with even larger population bases required, and the impact of growth of larger systems of care with their own quaternary capabilities, limiting referrals to UW Health.

The competition UW Health faces outside its traditional primary and secondary service area is from the five large systems mentioned earlier, which already are at least twice the size (as measured by clinical revenues) of UW Health ranging from $4 billion to $14 billion annually, and growing at a rapid rate, with inorganic growth being the main element. They also have large and growing footprints, surrounding Madison, and are growing closer. To be a force in this market, UW Health leaders believe the AMC needs to at least double its size and reach the current low end of the range of competitor sizes.

ACHIEVING SCALE

UW Health is in the early stages of its journey to scale up. Major initial activities in this process have included the following:

- *Detailed review of all markets:* We conducted a full opportunity and risk analysis throughout the relevant geography. The market was divided into 11 submarkets, and a full analysis was conducted in each. Certain submarkets were designated high priority for either offensive or defensive scale strategies.
- *Detailed review of existing relationships:* UW Health maintains strong relationships with many hospitals and physician groups. A few of these relationships are priorities for working toward a much higher degree of alignment in the short term, while a few others have great potential to be formalized and tightened in 2015 and 2016. UW Health is proceeding on multiple fronts to strengthen selected relationships.
- *Upgrading internal readiness:* Multiple scale-enabling efforts are under way along the lines of development and refinement and then implementation of guiding

principles, critical success factors, leadership commitments, and parameters for partnership. Of importance is the infrastructure being developed to support this major initiative

- establish a structure that can easily incorporate affiliates, including physician partners, which requires flexibility to accommodate diverse types of relationships;
- establish a structure for alignment with physicians outside of the traditional faculty practice plan model;
- create a streamlined decision-making processes bordering on "stay between the lines" or "single-signature authority" for network development executive and team designees;
- provide authority for staff involved in network development, including clear and streamlined reporting relationships;
- obtain clinical department chair buy-in and gain enthusiastic support, thereby diminishing and ultimately eliminating real or de facto veto power; and
- add or redeploy human resources to facilitate the above.

CONCLUSION

A review of various recent AMC approaches to addressing scale confirms the variability that seems to be inherent in all aspects of AMCs, in which no one strategy is best for all situations. A thoughtful and deliberate consideration of guiding principles, critical success factors, leadership commitments, and partnership parameters should facilitate the development of the best possible approach for a given AMC as it addresses and embraces the rapidly changing healthcare environment.

For more information about the concepts in this column, contact Mr. Zuckerman at AZuckerman@hss-inc.com.

VERALON™

HEALTHCARE MANAGEMENT ADVISORS

- Strategy and Planning
- Mergers and Transactions
- Valuation and Physician Compensation
- Clinical Transformation and Value-Based Payment

PHILADELPHIA CHICAGO NEW YORK WASHINGTON DC

www.veralon.com | 877.676.3600