Cost accounting definition:

Determining the estimated, standard cost of providing an individual healthcare service considering:

1. Direct Labor
2. Direct Supplies
3. Allocation of equipment and support costs
4. Allocation of the cost of all support services

Preparation

Cost accounting is not an off-the-shelf product, it's a time-intensive process.

1. Cost accountant meets with department manager to detail direct costs for every procedure in the department.
2. Cost accountant tries to estimate the amount of time each member of department spends on average for the same given case.

3. Cost accountant identifies use of major equipment to determine an effective cost per use.

4. Indirect costs are allocated based on overall volume in the department. **As volume goes down, cost per case goes up**. Full allocation of costs is known as the "cost profile." Must update twice annually to remain relatively accurate.
    a. Fixed (same cost regardless of volume)
    b. Semi-variable (typically, staffing if more than "core")
    c. Variable (like basic medical surgical supplies)

Best uses of cost accounting

1. Direct competition areas, particularly in urban locations. I have used cost accounting in two large systems; one in NC and one in Missouri.
2. Negotiations with commercial payers for rates of reimbursement where in a competitive area.
3. Identification of high priced/highly utilized supplies.

Costs of implementing a cost accounting system for a small hospital

1. Software: Varies by product; range $50-250K with additional 20% for annual support.
2. Staff: For small hospitals, 2 FTE with one highly sophisticated in Cost Accounting. Comp and benefits approximately $180,000/year.

Where cost accounting may not be effective

1. Cost data **works best when measuring procedures with a high rate of frequency**. A critical access hospital (CAH) like Porter may have 2000 admissions annually, but the distribution of the type of cases can vary widely.

2. **Small hospitals with a high percentage of fixed costs see much less return on an investment in cost accounting**.
    1. Porter's fixed costs are approximately 85-90%. Even a 5% reduction in volume can cause significantly higher cost per case.
    2. Many departments are small and require **minimum core staffing**, whether or not volume justifies that staffing on any given day.

Critical Access Hospital (CAH) Status

Porter Medical Center is a Critical Access Hospital in Middlebury, one of 8 in Vermont.

CMS created the CAH designation to ensure that small, geographically-challenged hospitals could remain stable and serve their communities, even with volatile patient volumes.

Hospitals that qualify for CAH status are reimbursed on a cost basis (instead of prospective payment or fee for service.)

To qualify as a CAH, a hospital has to agree to limit it's licensed beds and adhere to relative short average lengths of stay benchmarks – the result is that CAH hospitals provide essential services close to home, and leave complex care to larger hospitals.

Cost Control Strategies for Critical Access Hospitals

At Porter, we have addressed cost control in various ways this year, because we realize the very important work of reducing health care costs in Vermont, as well as better positioning Porter for success. As we reduce costs in any area, we reduce overall costs to our patients. A few examples:

1. Group Purchasing. Through support of UVM Medical Center, we were able to establish a Prime Vendor Contract with Medline at the tier pricing afforded to UVM Medical Center. This pricing would not have been available without their advocacy.

Cost Control Strategies for Critical Access Hospitals

2. Applied Management Systems (AMS). Staffing analysis per workload unit was evaluated for each department and practice. Sixty percent of all our expenses are salaries and benefits. All departments and practices were brought in line with recommended median levels, which reduced our overall expenses by $910,000 in this fiscal year.

3. Infrastructure. Our organization collapsed infrastructure for those services that are duplicated in Health Porter Nursing Home, the Porter Hospital, and the Porter Medical Group. As a result, we were able to attrition out management overhead and better integrate services and apply standard metrics of performance.

Cost Control Strategies for Critical Access Hospitals

4. Financial and performance metrics. Many benchmarks exist that help us gauge our performance relative to regional and national data bases from many hundreds of hospitals and physician practices. For example, we use MGMA (Medical Group Management Association) to measure our physician practices performance, salaries and utilization. These metrics have helped us know where to focus our work at Porter in reducing costs most effectively.