Seven Strategies that Provide Leverage for Increasing Profit

Implementing these steps can improve your bottom line.

BY JON A. HULTMAN, DPM, MBA

From our studies in physics, we all are aware of leverage—a mechanical advantage gained through use of a tool. For example, a simple lever allows us to move a disproportionately heavy object by applying a small amount of force. We can also apply the term "lever" to business strategies. In a medical practice, gains in revenue or treatment quality (goals achieved through "heavy lifting") might be accomplished through use of superior processes or "strategies." Effective processes are levers of sorts, and utilizing superior processes as levers can create disproportionate gains in profit, increasing any practice's bottom line. As the revenue of a well-run medical practice grows, its percentage of increase in profit outpaces its percentage of increase in revenue. This effect of magnifying profit in a positive direction is the result of "operational leverage"—leverage gained through the use of effective business strategies with the caveat being that the use of ineffective business strategies can magnify revenue changes in the negative direction.

In order to succeed in an environment in which prices are declining and costs are increasing, it is important for a doctor to understand the power of leverage. Here is an example of the term leverage as it applies to finances—in this case, the purchase of a home. Assume that we purchase a $1,000,000 home, investing $200,000 (20%) as a down payment. Our $200,000 investment is leveraged as the home price increases. When the home's value reaches $1,200,000 (a 20% increase), our $200,000 investment has grown 100%. In this case, our investment has provided us with significant financial leverage. Conversely, financial leverage can have a downside. If the value of this $1,000,000 home were to sink to $800,000 (a 20% decrease), 100% of our original investment would be lost. With the advantage of understanding the potential advantages and disadvantages of leverage, let us look at seven levers that doctors have at their disposal, tools that they can utilize to create positive financial and operational leverage for their medical practices.

1. Increase Fees

Raising prices has been the classic lever used by businesses to achieve immediate increases in revenue. Because a price increase does not increase expenses, 100% of the collected increase falls directly to the

Continued on page 152

Increasing Profit (from page 151)

bottom line as profit. As you know, the practice of increasing medical fees (other than ones for non-covered services) is no longer a lever at the disposal of doctors—with the exception of those who run concierge or cash-only practices. Negotiating better paying contracts is, however, an option—especially for doctors whose contracts' rates are based on documenting the achievement of better outcomes and higher levels of patient satisfaction—both of which can be achieved through sound business practices that enable quick access and short wait times.

2. Improve the Collection Ratio

Increasing the collection ratio presents a significant opportunity for greater revenue in most practices. Each patient visit can generate numerous tiny business transactions. As a result, as patient volume grows, transactions increase exponentially, making it easy for the number of mistakes in the practice to be magnified and for data (both clinical and business) to go uncaptured or "fall through the cracks." One simple data entry mistake, or one piece of data "falling through the cracks," can result in an under-payment—perhaps, even no payment. Sometimes, growth also creates delayed collections. The longer accounts remain in receivable, the lower the collection ratio. Again, sound business processes will lessen the opportunity for these errors and inefficiencies to occur. Similar to the practice of increasing fees, each percentage improvement in the collection ratio is "found money" that drops directly to the bottom line. No practice collects 100% of allowable charges, but establishing efficient business practices will lead any practice to a higher collection ratio.

3. Increase Patient Volume

As we know, increasing patient volume increases revenue. This "lever," however, also increases costs. If there are significant inefficiencies in practice processes, increasing volume will simultaneously lower service quality by increasing patient wait times. The greatest leverage associated with volume increases occurs in practices in which any increase in patient or service volume is spread over relatively fixed costs. Once fixed costs are covered, the main new costs associated with volume increases are the variable ones needed for supplies. In an efficiently run practice, the end result of increased volume is a significantly higher profit margin, per visit, for any new patient.

Increasing the collection ratio presents a significant opportunity for greater revenue in most practices.

4. Increase Service Volume

Many busy practitioners—especially those who are understaffed—tend to focus on the chief complaints of their patients. Because these doctors are rushed, they are less likely to provide additional services or to follow-up on secondary complaints. Often, a patient's secondary complaints are the ones that have been chronic. More painful chief complaints are what have eventually motivated these patients to actually schedule visits. This tendency for doctors to neglect following up on secondary complaints can be detected by calculating the number of CPT codes he/she bills, per visit. The closer this number is to 1.0, the more likely it is that the doctor has little time to provide all the necessary services to help his/her patients. The number of CPT codes billed by the average DPM is around 2.0 per visit. Obviously, operating an efficient practice that allows the doctor ample time per patient will enable him/her to provide all the services that a patient needs. This, in turn, will provide leverage for both improved patient satisfaction and the practice's bottom line.

Because these doctors are rushed, they are less likely to provide additional services or to follow-up on secondary complaints.

5. Reduce Costs

The leverage provided by reducing costs is especially strong in practices that have grown steadily in volume without addressing inefficiencies—practices that have allowed an accumulation of unnecessary costs to mount. In a mature, price-competitive market such as we have today, a significant emphasis should be placed on increasing efficiency and eliminating unnecessary costs. Overhead is a necessary cost for providing medical services and producing revenue, but overly high overheads are typical and represent a significant burden for doctors. Knowing that controlling expenses does not require "being cheap" or putting off investing in a practice. One of my favorite axioms is, "You can't cut your way into prosperity." Control is not simply cost-cutting; it is selectively spending on items that, or people who, will increase quality and/or provide returns that are greater than their cost. Expenses that do not accomplish this end are wasteful, add no value, and should, therefore, be eliminated. Identifying unnecessary expenses and controlling them during periods of growth is healthy for a practice. This will provide greater profit leverage than that created by a much larger increase in revenue.

6. Merge Practices

Done correctly, practice mergers can provide significant leverage for increasing profit because they reduce overhead ratios, which in turn reduce the average cost-per-patient visit. A merger is especially effective when two practices merge into one facility

Continued on page 154

Increasing Profit *(from page 152)*

and focus on building efficient processes. While mergers that create larger groups and networks are popular today, the greatest leverage is achieved when two solo or small group practices are merged into one. While it is common to see small practices with overhead ratios of 60% or even higher, a merger could easily reduce such a ratio to 40%. This decline in a practice's overhead percentage would increase compensation by 50%. For example, a practitioner with a 60% overhead who is collecting $400,000 will take home $160,000. Reducing this overhead to 40%, this same practitioner will take home $240,000—50% higher than $160,000. It is hard to imagine that more solo practitioners do not take advantage of this opportunity to earn 50% more without adding volume, working more hours, or for that matter, making any changes other than merging their practices. Some doctors say that they enjoy their independence, but a 50% increase in profit is hard to disregard given that the participants in a merger will still be relatively independent—especially when compared with employed physicians.

7. Increase Productivity

There is a wide range of productivity among doctors—even ones working in the same practice. Increased productivity provides significant leverage for increasing revenue—especially for a very busy practitioner who is not necessarily interested in increasing his/her volume. Rather than reducing costs, the correct strategy is, sometimes, to spend more. Expenses such as adding an associate, expanding the number of treatment rooms, or hiring a staff person in the clinical area to assist the doctor or serve as a scribe should be seen as investments. These investments pay dividends by expanding the amount of time the doctor has available to provide patient care—leading to greater productivity per hour.

Each of the seven levers listed above can be used individually and independently to improve your bottom line. Can you imagine the potential leverage available to a practitioner who employs all seven of these levers simultaneously? This certainly is possible. And one last thought: once these strategies are implemented, they are most likely to be continued going forward if a practice is able to measure its progress in each area as it advances along this journey. **PM**

Dr. Hultman is Executive Director, California Podiatric Medical Association, President, Medical Business Advisors, specializing in practice evaluations, valuations, and mergers. He is the author of Reengineering the Medical Practice and Medical Practitioner's Survival Handbook