Outsourcing Business Processes

Here's a fresh look at this concept.

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Those who know me know I am a perpetual microeconomics student. Call me crazy, but I just have a particular affinity for the subject. This article will discuss the microeconomic principle of "opportunity cost" and hopefully help you understand its relevance to your practice and decisions to outsource some essential functions.

As economic pressures gain a grip on medical practices and stress their resources, addressing the concept of opportunity cost and outsourcing becomes instrumental. Outsourcing is a business practice in which services or job functions are performed by a third party on a contract or ongoing basis. More specifically, business process outsourcing (BPO) is a term used for outsourcing a specific business process task, such as payroll, billing, marketing, etc. A few of the more relevant advantages of outsourcing include lower costs (due to economies of scale or lower labor rates), increased efficiency, increased focus on core competencies, and access to technical skills or resources.

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Some potential pitfalls to outsourcing might include slower turnaround time, lack of business knowledge, language and cultural barriers (if offshore), and lack of control.

Recall from my previous articles that an "opportunity cost" is the cost of an alternative that must be forgone to pursue a specific action. Put another way, it's the benefits you could have received by pursuing an alternative activity.

Medicine is rapidly becoming a hybrid of medical care (patient care) and non-medical care (business management, billing, marketing, etc.). Unfortunately, we cannot devote time to one without sacrificing time dedicated to the other unless resources are unlimited, which is highly unlikely. That is the applicable opportunity cost.

Production Possibility Frontier (PPF) Curve

Economists use what's known as a Production Possibility Frontier (PPF) curve to explore where maximum growth potentials exist between alternatives.

Using medical billing as an example (but you can use any business process here), Figure 1 might be a PPF curve for Acme Podiatry (fictional). It demonstrates the "something has to give" concept of opportunity costs when examining the decision to outsource.

Sticking with the example of medical billing, let's now consider the true costs associated with the billing process of a medical practice. According to national averages, a full-time biller costs approximately

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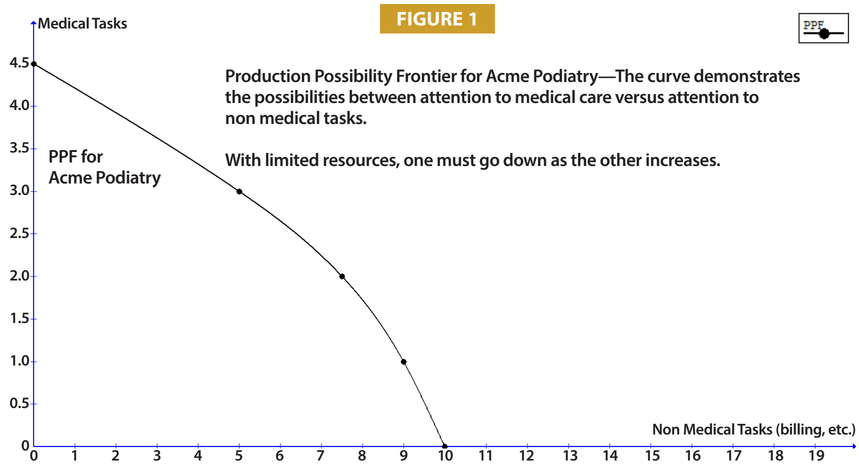
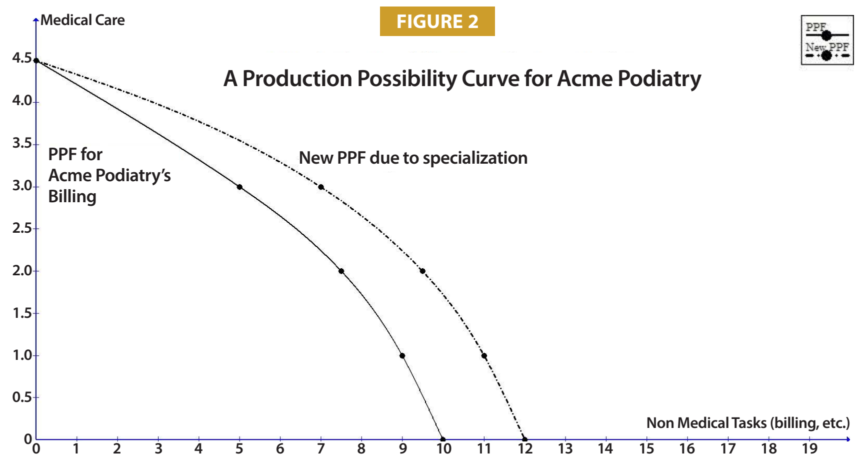
$45,000 per year (salary, taxes, benefits) and a full-time biller is required for each $600,000 in collections. So a practice generating $1.2M in collections would typically require two full-time billers. Using these national averages, the cost of the billers related to collections would be 7.5% ($90,000/$1.2M).

But that accounts for only the human resource cost. We must also consider the cost of technology, training, office space, etc. Just as the PPF curve explains the opportunity cost associated with medical care versus non-medical care, there are opportunity costs associated with all the additional biller expenses just noted. The total cost of billing could easily climb to over 10-12% of collections!

And what if the billers were not specialized, or they also handled other tasks within the practice? What if they needed to be trained more to work as accurately and quickly as possible? The costs go up exponentially.

The real objective of maximizing growth is NOT achieved by “moving along” a PPF curve and giving up something to gain another. The real growth comes from “shifting” the PPF curve outward through “specialization of labor”, which requires outsourcing.





Because an outsourcing strategy was deployed, nothing was sacrificed when more attention was placed on billing.

Changing the Curve

In the PPF curve in Figure 2, Acme Podiatry decided to outsource their billing to “highly specialized and trained” billers. They did so for barely the cost associated with ONLY their current total billing costs. But this specialization allows for an outward shift of the PPF curve so that at any given point of medical care, attention to non-medical care tasks (which can potentially create even more revenue and quality) are much greater. Now that’s true economic growth!

In the example above, because an outsourcing strategy was deployed, nothing was sacrificed when more attention was placed on billing. Essentially, a new PPF curve was born.

Whether you are considering billing, marketing, IT tasks, etc., what does it really cost you to perform a business process in-house? It’s essential that you consider the following:

- Human resources (salary, benefits, and taxes)
- Technology (computers, etc.)
- Physical opportunity cost (office space in square feet x cost per square feet)
- Human opportunity cost (losses on time spent on non-medical care)
- Human error associated with non-specialization.

So the next time you entertain the thought of outsourcing a business process, always keep in mind the Production Possibility Frontier Curve and truly know your current costs and opportunity costs. **PM**

Dr. Guiliana is a nationally recognized speaker and author on topics pertaining to medical practice management. He is a Fellow of the American Academy of Podiatric Practice Management and holds a Master’s Degree in Healthcare Management. He has authored numerous columns in various journals and is the co-author of *31½ Essentials to Running Your Medical Practice, as well as The Million Dollar Practice…Keys to Success.* Dr. Guiliana is currently a Medical Director of Podiatry for Modernizing Medicine’s award-winning technology. He can be reached at John.guiliana@modmed.com.