

## **EXSUM US Health Systems:**

### **Administrative Complexity & Waste in the US Healthcare System**

#### **Question:**

How does administrative complexity and waste influence costs associated with healthcare delivery, finance, reimbursement, and payment?

#### **Domain/Competencies:**

Health Resource Allocation

Performance Measurement & Improvement

**Method of research/Model:** This literature review of books and peer-reviewed journals identified through Google Scholar and Baylor OneSource applied the Health Care Parity Model study to articulate challenges and the key factors influencing the administrative complexities and waste associated with expenditures in the United States healthcare system. Understanding why healthcare organizations in the industry incur high administrative costs due to complexity provides healthcare administrators better insight on opportunities to eliminate waste and control the costs of healthcare in America. The results of the research outline the major contributing factors of administrative complexity on the costs associated with the functions of finance, delivery, payment, and reimbursement of healthcare; the process factors influencing administrative complexity; and process waste associated with the administrative complexity in the US healthcare system.

#### **Overview:**

Understanding why healthcare organizations in the industry incur high administrative costs due to complexity provides healthcare administrators better insight on opportunities to eliminate waste and control the costs of healthcare in America. The results of the research outline the major contributing factors of administrative complexity on the costs associated with the functions of finance, delivery, payment, and reimbursement of healthcare; the process factors influencing administrative complexity; and process waste associated with the administrative complexity in the US healthcare system.

Over the past few decades, healthcare costs in America have risen sharply. The degree to which healthcare spending consumed the economy in terms of Gross Domestic Product (GDP) doubled from 8% to 16% between 1975 and 2007, and is expected to reach 20% of GDP by 2016 (Orszag & Ellis, 2007). Administrative costs alone represent a significant portion of healthcare costs and accounted for an estimated \$156 billion in 2007 and are on a trajectory to reach \$315 billion by 2018 (Yong, Saunders, & Olsen, 2010). *Muda* is the Japanese word for “waste” and the types of waste identified in lean thinking include transportation, inventory, motion, waiting, overproduction, over-processing, and defects (Womack & Jones, 2010). Correlating administrative overhead costs with these types of waste can assist healthcare administrators to identify which business processes can be streamlined or eliminated to maximize value and contain growing healthcare costs within their organizations. In terms of value, administrative costs incurred by health care organizations which do not positively influence quality may present

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healthcare administrators opportunities to improve their operations. Therefore, it is important for healthcare administrators to understand how administrative complexity influences administrative costs associated with healthcare delivery, finance, reimbursement, and payment and be able to identify wasteful business processes that increase administrative costs.

### **Findings:**

- Interactions between providers and insurance is a major cost (\$31 billion)
- Interactions include:
  - gaining prior authorization
  - working with formularies for medication
  - processing insurance claims
  - maintaining their credentials
  - contracting prices with a multitude of insurers. High degree of variance.
- \$68,274 per physician per year

### **Single-Payer vs Multi-payer Systems**

- Lower interaction variance in Single-payer system, such as National Health Insurance in Canada
- US spends \$82,975 per physician per year, other overhead costs considered
- Canada spends \$22,205 per physician per year
- $\Delta$  \$60,000 per year per physician

### **Administrative Complexity & Muda**

- 34% of healthcare expenditure is waste
- 50% of Administrative Costs in healthcare are waste
- \$183 billion per year in Billing & Insurance-Related (BIR) waste

### **Lessons Learned:**

The Institute of Medicine (2010) discusses two categories of waste associated with interactions: *unnecessary interactions* and *inefficient interactions*. Unnecessary interactions are those where the marginal cost exceeds the marginal benefit of the interaction, are non-value add, and need not be performed; whereas, inefficient interactions are the tasks performed in a manner that do not realize maximum net benefit and, therefore, create waste (IOM, 2010). However, the literature does not specifically define what parts of these interactions are value-add and which are administrative muda.

Research in this area is stifled due to the vast array of administrative processes and largely undefined field of administrative costs (IOM, 2010). Research that attempts to clarify the definition of administration is pivotal to distinguishing between value added spending and wasteful expenditures (Pozen & Cutler, 2010). The topic needs further research to effectively

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define and stratify administrative costs in the US health system. Significant gaps in research linking administrative complexity to the various types of waste present in the US health system remain. Research providing empirical data from lean projects focusing on reducing or eliminating inefficiencies and redundancies in the spectrum of administrative complexity will assist healthcare administrators in their efforts to improve the US health system. Furthermore, specific research regarding administrative costs and waste in the Military Health System does not exist.