Reed Tinsley, CPA

The 12-Step Way to Reduce Practice Expenses:

PART 2, OPERATIONAL EFFICIENCIES

Even small cuts in your operational expenses can add up to big savings for your practice.

As you probably know from experience, money can easily leak out of your practice, both through obvious holes that you haven't gotten around to plugging and through cracks you haven't even noticed yet. In these days of tightening reimbursement for medical care, you simply cannot afford a financially leaky office.

In the typical family medicine practice, overhead consumes about 60 percent of net revenue.[1] Reducing practice expenses is one way to reduce your overhead percentage. It requires a disciplined, methodical approach, such as the 12-step, 12-month plan proposed in this series (see "The 12-month plan at a glance," page 32). The first article in this series ("The 12-Step Way to Reduce Practice Expenses: Part 1, Staffing Efficiencies," March/April 2010, page 38; http://www.aafp.org/fpm/2010/0300/p38) looked at staff-related expenses, such as salaries and benefits. In this article, we will scrutinize a variety of other practice expenses that deserve your attention.

Month 6: Lease agreements

Does your office lease account for about 6 percent of net revenues? That's typical for family medicine practices. If you are paying more, study your lease, looking for hidden costs.

The first item to review is your *operating stop* provision. Under the typical operating stop provision, the landlord agrees to pay a base amount toward the building's operating costs and allocates any excess costs to the tenants. This means that, even though you agreed to pay a specific rental rate per square foot of space, the actual amount you pay the landlord may increase each year because of the operating stop provision. Therefore, it's important to review the specific costs the landlord includes in the operating stop calculation. Look for costs that have nothing to do with the building's operation, such as unrelated payroll costs and management fees. Ask your accountant to audit the landlord's operating stop calculation each year, and challenge your landlord about any irregularities.

Even if the lease contains no hidden expenses, it may still represent a waste of money if you're paying for more space than you need. Is your office space designed as efficiently as possible? Are you renting space you might someday grow into but don't anticipate using in the immediate future? If so, consider renting out part of the space, if that's feasible. And are you paying for more of the building than just your office? There is a difference between net *rentable* space and net *usable* space in a lease agreement. Net rentable space allocates to you your share of common space in the building. So, if you rent space in a building that has a beautiful atrium, you pay for part of this unusable space. Ask yourself how important that space is to you.

Also, check the lease to see whether the landlord requires your practice to purchase certain types of insurance or specific coverage limits. Are they really necessary? Are there alternatives? Although you may be unable to renegotiate these issues in the middle of a lease, you can address them before you sign a new one.

And you might as well ask yourself the big question: Would it be cheaper in the long run to own a building than to rent office space? Look into some available buildings, and compare your lease payments to how much it would cost monthly to own a building, taking mortgage, down payment and upkeep expenses into consideration. Also, if your practice has more than one location, you might want to consider consolidating them, which could save you rental fees and produce other economies of scale.

While you're at it, review all other lease agreements, especially equipment leases. Many practices prefer leasing to buying because they can immediately deduct the rental fees on their taxes instead of depreciating the assets over time. But depending on the interest rate and end-of-lease purchase requirements, it might be cheaper to purchase certain items.

Examine all maintenance contracts on office equipment as well. Can you negotiate maintenance with the rental company? Can you acquire the same maintenance contracts elsewhere but for less expense? Are the maintenance contracts necessary in the first place? Many practices pay for maintenance contracts for equipment that lost its value long ago or is seldom used.

Finally, analyze repair costs on the practice's equipment, furniture, fixtures and leasehold. Were these repairs necessary? Are they likely to occur again on the same asset? Should you allocate resources to purchase new assets rather than continuing to repair them?

Action steps: Audit your lease agreement and challenge the landlord about excess operational costs. Review how space is used in your suite and consider renting out excess space. Consider the relative merits of buying and leasing. Review your equipment leases, maintenance contracts and repair costs.

Month 7: Costs of medical and office supplies

For a family medicine practice, medical, drug, laboratory and office supply costs average anywhere from 8 percent to 10 percent of revenues. To assess your own supply costs, start with some comparison shopping. If you have locked yourself into doing business with one vendor, especially for medical supplies, you may not be getting the best price available. You'll generally do better if you develop a list of the supplies you use and send the list to a number of vendors for bids. (Visit http://aafpbuyersguide.com for a list of vendors.)

One way to save on supply costs is to seek out group purchasing opportunities, which can give you volume-discount prices. For example, practices save an average of 25 percent to 35 percent when they purchase vaccines

About the Author

Reed Tinsley is a Houston-based CPA, certified valuation analyst and health care consultant. Author disclosure: nothing to disclose.

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By scrutinizing practice expenses one at a time, you are likely to find inefficiencies that, if addressed, could save you money.

For starters, look for hidden costs in your lease, evaluate your office space requirements and consider the merits of buying.

When you purchase supplies, always comparison shop; don't rely on the same vendor year after year.

through a purchasing cooperative.[2]

You may also be able to save on supply costs by printing some things yourself. For example, does your computer system have the ability to generate a superbill or patient charge ticket that's just as good as the one you now purchase? Could you generate your own patient education materials or other office forms? Printing your own might save you money, particularly if you shop around for the best toner and paper prices. Note, however, that for high-volume printing it can be cheaper to print forms professionally than to use a copier each time.

No medical office can afford to over-purchase and waste supplies. Review your inventory at the end of this month and monthly thereafter. If it remains high or increases, limit the amount of supplies your office purchases each month. Does your office have a clear purchasing policy? If not, do the following:

- Specify how staff will determine what supplies to order each month,
- Identify *one* staff member who will be in charge of purchasing – and accountable for responsible purchasing and management of supplies,
- Give that staff member authority to collect requests for supplies, shop for the best prices, place orders, check items received against original orders placed and inspect all related vendor invoices.

To give this person an incentive to do a good job, you may want to set a goal for them (e.g., "Reduce annual supply costs by 2 percent") and offer a bonus for meeting that goal.

If your practice has multiple offices, consider centralizing authority for purchasing supplies in one location and standardizing the supplies used as much as possible. Then arrange for delivery of supplies to each office site. Offices may need to share supplies with one another to cover shortfalls, but don't allow any office to order more supplies on its own.

Action steps: Seek competitive bids for supplies. Seek group purchasing opportunities. Assign one staff person to monitor supplies. Centralize purchasing authority. Consider generating your own forms rather than purchasing them.

Month 8: Outside services

Do you inspect expenses related to professional fees from time to time? Are these expenses really necessary? Separate the one-time costs from the ongoing costs. With ongoing professional fees, search for less expensive alternatives. For example, a practice may hire an outside firm to administer its retirement plan, not realizing that the accountant who does the practice's taxes might be able to perform the service for less. The same applies to costs for ancillary services such as laboratory and radiology. If you pay an outside company for such services, ask yourself whether similar companies could provide the same service for less. Get competitive bids.

THE 12-MONTH PLAN AT A GLANCE

IN THE PREVIOUS ISSUE >>	**Month 1:**	Review staffing needs and adjust staff size if necessary.
	Month 2:	Assess and systematize staff compensation.
	Month 3:	Look for savings in health insurance.
	Month 4:	Review your retirement plan for potential savings.
	Month 5:	Develop or refine your sick leave, vacation and overtime policy.
IN THIS ISSUE >>	**Month 6:**	Review your office lease and other lease agreements.
	Month 7:	Optimize the ordering and handling of supplies.
	Month 8:	Scrutinize the cost-effectiveness of outside services.
	Month 9:	Look for ways to economize on postage and telephone costs.
	Month 10:	Review your practice advertising for waste and ineffectiveness.
	Month 11:	Track down and eliminate causes of refunds to patients.
	Month 12:	Tighten controls on petty cash and eliminate problems that incur bank charges.

>> Practices save an average of 25 percent to 35 percent when they purchase vaccines through a purchasing cooperative.

If you contract with an outside collection agency, is the cost of paying the agency worth the amount of recovered revenue? Compare the net amount collected by the agency (total collections less the agency's fee) to an estimate of what you would net if you were handling collections internally (total anticipated collections less the cost of personnel, equipment, paper, postage and decreased office efficiency).

Other costly services include insurance for your building and its contents and malpractice coverage. Bid out building-and-contents insurance periodically to make sure you are getting the best coverage for the best rate. For malpractice insurance, you may be able to lower your rates by purchasing coverage through a medical organization or group affiliation, such as an IPA.

Action steps: Seek cheaper alternatives for professional services. Evaluate the cost-effectiveness of bringing functions in-house. Bid out office insurance, and look for less expensive malpractice coverage.

Month 9: Postage and telephone costs

Postage and telephone costs in a medical office are rarely controlled. Do your employees use office postage for personal correspondence? To plug this leak, assign one person in your office the responsibility for coordinating mail services, someone who will enforce an office-only mailing policy. How much of the correspondence from your office to the outside world is unnecessary? For example, do your patients receive redundant communications from you? Perhaps your practice would benefit from some type of metered system. Can you double up on mailings? You may be able to save money by including other necessary communication with bills so that you send one envelope instead of two.

A small amount of investigation might reduce your telephone costs, too. Does your office pay for telephone lines or other options that it does not use? Have you bid out your answering and paging services lately in search of the same services for less? Can your telecommunications system detect whether employees are making personal long-distance telephone calls? These things add up.

Action steps: Develop an office mailing policy. Assign one staff member to monitor mail and to seek mailing efficiencies. Assess telephone service. Implement cost-efficient phone alternatives.

Month 10: Advertising

Critique the cost and related benefits of advertising your office's services. Many offices spend money on advertising and similar marketing ventures that yield them little benefit. Look first at any costs related to display advertising, especially in the Yellow Pages, both the print and online versions. Many offices pay for advertising in not one but several telephone directories, an action that can cost thousands of dollars per year needlessly. Do you need to advertise in the Yellow Pages at all, other than merely listing your name, address and phone number? Most health plans and hospitals publish directories that patients find more useful than the phone book. And what about advertising your practice on items such as calendars or pens? Ask yourself whether it does anything for your practice. Can you tell whether it pays for itself?

If your new-patient questionnaire doesn't already include a question such as "How did you hear about us?" consider adding one, giving check-off options that include the media where you advertise as well as referrals from patients and other health care professionals; at least you'll get an indication of how well the money you are spending on the Yellow Pages and other advertising is working for you. If you find that a given advertisement doesn't generate twice its cost in revenue, it's probably not worth keeping. ➤

Identify one staff member who will be in charge of purchasing and managing all the supplies for your practice.

If you are paying a hefty bill for outside professional services, evaluate the cost-effectiveness of bringing those functions in-house.

Your practice can lose a surprising amount of money from uncontrolled postage and telephone expenses.

>> Do you know where your petty cash disbursements go?

Action steps: Assess advertising. Eliminate ineffective advertisements. Develop more effective alternatives.

Make sure any advertising you do benefits your practice enough to justify the cost.

Month 11: Refunds to patients

Refunds to patients are usually listed in the revenue portion of the income statement, where they are deducted from the practice's gross collections, so this may be an expense your practice overlooks. By reducing refunds to patients, you can increase your practice's net income.

Together with your business office staff, examine factors that cause refunds and eliminate them. Select a few patient accounts that have required a refund and trace the transactions through your billing and collection system. By doing this, you will see whether the refunds happened because of human error (such as posting a payment incorrectly) or systems error (such as having the wrong co-payment amount in the system).

Action steps: Assess patient refunds. Initiate a system to reduce patient refunds.

If you find yourself giving refunds to some patients, find out why and put an end to the problems that result in refunds.

Month 12: Petty cash and bank charges

Track your nickel-and-dime expenses. For example, do you know where your petty cash disbursements go? When the pizza delivery driver shows up, do you pay him from petty cash and never record where that money went? If you don't record these disbursements, you'll reach in the money drawer one day and find the petty cash gone. And are your petty cash disbursements really necessary? Petty cash may be another responsibility to assign to one trusted staff member for close monitoring.

No practice should incur bank charges and penalties; if your practice does, you are throwing money away.

Bank charges and penalties are other hidden overhead expenses, ones no medical office should ever incur. For example, you may be penalized for a late payroll tax deposit or tax form mailing. Or you may receive a bank charge because your account does not maintain a minimum balance each month. Take whatever steps necessary to stop these avoidable expenses.

Action steps: Set up a system to monitor petty cash. Eliminate extra bank charges.

Keeping more of what you earn

Your practice's financial success is determined not only by what you earn but also by what you keep. These 12 steps will help you reduce your practice expenses and keep more of what you earn. You can address them one at a time, one per month over the course of a year, or divide the 12 steps among the leaders in your practice and reduce your costs even sooner. Either way, you will realize a boost to your bottom line – without having to work harder or longer each day. FPM

Send comments to **fpmedit@aafp.org.**

Editor's note: FPM *was published for several years before going online. In an effort to capture the best of the "pre-web"* FPM *for the online archive, we are publishing updated versions of some particularly useful early articles. The original versions of this article and a companion article in the March/April 2010 issue, which provided advice on reducing staff-related expenses, first appeared in 1997.*

1. *Cost Survey for Single-Specialty Practices: 2009 Report Based on 2008 Data.* Englewood, Colo: Medical Group Management Association; 2009.

2. Moore KJ, Hughes C, Stone T. Vaccination management: Is your practice on target? *Fam Pract Manag.* September/October 2008:28-31; http://www.aafp.org/fpm/2008/0900/p28.html.

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