Bad debt, the profit killer

– Jim Musslewhite, president, Oncology Convergence, Inc.

During the past several months, the tenor of the conversation in the oncology community has shifted, focusing on the economy and its impact to health care and oncology infusion. Several oncology practices have experienced an increase in uninsured and underinsured patients, meanwhile other practices have reported an increase in medical bankruptcy filings. Current economics aside, another unexpected increase in bad debt is due to some self-funded and county-funded insurance plans that are having an increasingly hard time paying their claims due to a lack of financial resources.

The lack of financial resources for both the patient and insurance companies impact an increase in bad debt, or what I define as write offs or uncollectible revenue. Many practices, due to the factors listed above, are experiencing increases in their percentage of bad debt write offs based on a percentage of their collections. This is occurring at the same time all practices have seen decreases in their reimbursement for the administration of drugs from Medicare and all plans that base their reimbursement on Medicare's rates. Additionally, many payers are employing edits and other tactics, causing delays to payment. The result is a dramatic impact on cash flow and profitability. On top of these current conditions are numerous other reasons for practices to experience increased levels of bad debt, including higher co-pays, increased co-insurance and an increase in deductibles.

This is not an issue isolated to oncology, according to Fitch Ratings. Fitch states: "Overall, Fitch expects deteriorating collections and growing numbers of uninsured patients to result in industry-wide increases in bad debt expense and uncompensated care in 2009."[1] Additionally, Fitch Ratings' For-Profit Hospital Industry Quarterly Diagnosis for the first quarter of 2008 states that the average bad debt expense for hospitals for profit was 17.7 percent.[2] As Table 1 illustrates (below), if our fictitious practice had bad debt levels in the high teens, they would be subsidizing the health care system to the tune of $400,000-$500,000 per year. Let us look at an example of the financial impact of bad debt to a fictitious 100 percent Medicare single-doctor practice

Table 1: Impact of bad debt

	1% Bad Debt	2% Bad Debt	5% Bad Debt	10% Bad Debt	20% Bad Debt
Gross Charges	$8,000,000	$8,000,000	$8,000,000	$8,000,000	$8,000,000
Charges for Professional Services	$2,000,000	$2,000,000	$2,000,000	$2,000,000	$2,000,000
Contractual Adjustments	$1,000,000	$1,000,000	$1,000,000	$1,000,000	$1,000,000
Bad Debt Writeoffs	$10,000	$20,000	$50,000	$100,000	$200,000
Revenue from Profession Services	$990,000	$980,000	$950,000	$900,000	$800,000
Charges for Drug Infusion	$6,000,000	$6,000,000	$6,000,000	$6,000,000	$6,000,000
Contractual Adjustments	$3,000,000	$3,000,000	$3,000,000	$3,000,000	$3,000,000
Bad Debt Writeoffs	$30,000	$60,000	$150,000	$300,000	$600,000
Revenue from Drugs	$2,970,000	$2,940,000	$2,850,000	$2,700,000	$2,400,000
Drug Costs (2% margin)	$2,940,000	$2,940,000	$2,940,000	$2,940,000	$2,940,000
Profit/(Loss) from Drugs	**$30,000**	**$0**	**($90,000)**	**($240,000)**	**($540,000)**

Assumptions: Professional and Administrative Services account for 25% of charges, drugs 75%. The drug margin from Medicare is 2% (this number is obviously based on each practice's acquisition price). Operating costs are excluded from this example due to the variability inherent in each practice. The practice is 100% Medicare for the purpose of this example.

and the yearly impact that increases in bad debt can have to the profitability of the practice. For simplicity's sake, we will use a fee schedule set at 200 percent of Medicare's allowable and an actual margin on drugs for Medicare of two percent (the approximate margin for many high priced drugs). Table 1 illustrates the impact to profitability as the percentage of bad debt increases.

Most practices do not have separate adjustment codes for bad debt, uncovered diagnosis, bad demographics or any insurance contractual adjustments. This creates an inability to distinguish, and therefore report on the reasons for the adjustments. For the sake of our example, let us assume that the average practice is successful in collecting 75 percent of the Medicare 20 percent patient burden for treatment. If this fact were to be the case, then the average practice has a bad debt percentage of five percent for Medicare, which would translate (based on our example above) into a loss of $90,000 in drug expense each year.

To look at the impact of bad debt from another perspective, if the practice wrote off an uncollected patient balance of $4,500 due to a medical bankruptcy, death, or any other reason the practice would have to perform and collect 100 percent of $450,000 in services to just "make up" the $4,500 loss. ($4500/.02 = $225,000 in cash or $450,000 in gross charges).

The battle against bad debt is won or lost before the patient ever sits in the infusion chair. The common causes of bad debt are: uncollected patient responsibility, off-label drug usage, daily insurance maximums (a growing problem), and unrecognized changes in insurance status (lack of continual re-verification). These issues are all identifiable before the patient receives treatment. Then the decision is made with a complete picture of the patient's insurance and financial standing based on the treatment protocol and the cost estimate. The practice can then make a decision on treatment alternatives and proactively establish payment plans, enroll in patient assistance plans for assistance with drugs and co-pays, or inform the patient they will need to be treated elsewhere. Whatever decision the practice and the patient collectively make, the difference is profound. The patients are made completely aware of their financial responsibilities and the practice protects its bottom line and therefore its ability to treat the next patient with the same level of care and compassion that all of the patients deserve. H

References

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2. "Bad debt expense drops at for-profits for Q1 '08, Fitch says" Fierce Health Finance http://www.fiercehealthfinance.com/story/bad-debt-expense-drops-at-for-profits-for-q1-08-fitch-says/2008-05-28

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