

RI's Hospitals Need to be More Transparent About Prices, Income, Spending, and Efficiency

Lacking these numbers makes it impossible to assess the value hospitals deliver to employers and consumers

A report from the Rhode Island Business Group on Health

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Rhode Island's hospitals are like much of the hospital industry nationwide in that almost all have a stunning lack of transparency regarding their prices, sources of income and spending. Such opacity hinders any comprehensive assessment of whether hospitals in the United States—including those in Rhode Island—are becoming more or less efficient.

The issue of hospital efficiency is critically important in Rhode Island because hospitals are the largest expense included in medical claims that commercial health insurers pay on behalf of employers, unions, families, individuals, cities and towns and the state government itself. Therefore, assessing the overall financial performance of hospitals is necessary to understand the effect hospitals have on commercial health insurance premiums in Rhode Island. After all, the efficient use of resources is essential for making health insurance more affordable, and affordability is a key component of the value hospitals deliver.

A Focus on Revenue or Value?

As industry experts point out, the growing \$200 billion hospital revenue-cycle-enhancement business is an indication of an industry more focused on boosting income than on delivering value-based care. Consider, for example, [this comment from David W. Johnson](#), a hospital consultant and member of the Healthcare Financial Management Association board of directors who said during an investor forum that half of hospital CEOs admitted that their asset-heavy business models were not sustainable. “Most CEOs agreed that their operations required a major overhaul to remain competitive,” he explained, adding, “Houston, we have a problem!”

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In our previous report, [“Hospitals’ Rising Overhead Costs Erode Efficiency,”](#) RIBGH compared hospital overhead costs in Rhode Island against that of hospitals in other states. When expressed as a percentage of total expenses, Rhode Island hospitals’ overhead costs are second highest in the nation. In this report, we are diving deeper into these costs.

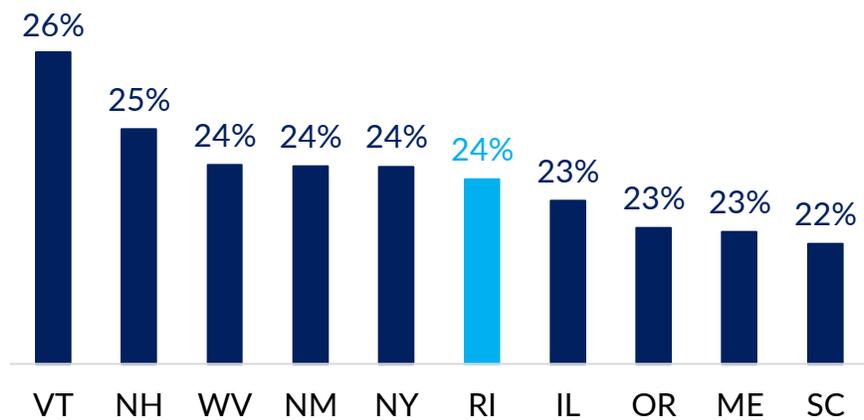
In-hospital spending on overhead is also called general service or non-revenue-producing departments. In large hospitals, overhead can include 25 or more departments, including cost centers for administration and general services, employee benefits and capital expenditures. When compared with the other overhead departments in most hospitals, this bundle of administrative costs typically accounts for the largest expenditures and the highest year-over-year increases in overhead.

The Main Sources of Overhead

Also included in the hospital overhead category are department-level hospital expenses and outside expenses brought into the hospital. The latter includes costs from health systems and related organizations. There are also categories of expenses that Medicare designates as non-reimbursable cost centers, which include physicians’ private offices, research, gifts, coffee shops and advertising.

Improved transparency into these spending areas would allow the public to assess hospital operations more closely. One way to do so would be to evaluate overhead costs in an administrative bundle of services that would include administration and general, employee benefits, capital, and other services expressed as a percentage of total expenses. Exhibit 1 shows that these costs in Rhode Island’s hospitals are the sixth highest in the nation.

Exhibit 1: High Overhead Operating Costs
Rhode Island’s hospitals have the sixth highest operation costs in the nation



Source: Cost Reports, Centers for Medicare & Medicaid Services

All hospitals face rising expenses not only from the cost of providing direct patient care but also from the growing financial costs that health systems impose on individual hospitals. Over the past 12 years, the costs associated with operating six health systems in Rhode Island have increased significantly, encompassing such expenses as developing partnerships with physician groups, rising administrative expenses, and operating retail pharmacies inside hospitals. The trend toward rising costs requires a broader discussion of the urgent need for hospitals to reassess their business models to ensure long-term financial stability.

A Warning from Consultants

“Health systems should target cost reductions of 15%-20% by 2030. That means balancing near-term operations optimization with long-term transformative efforts”

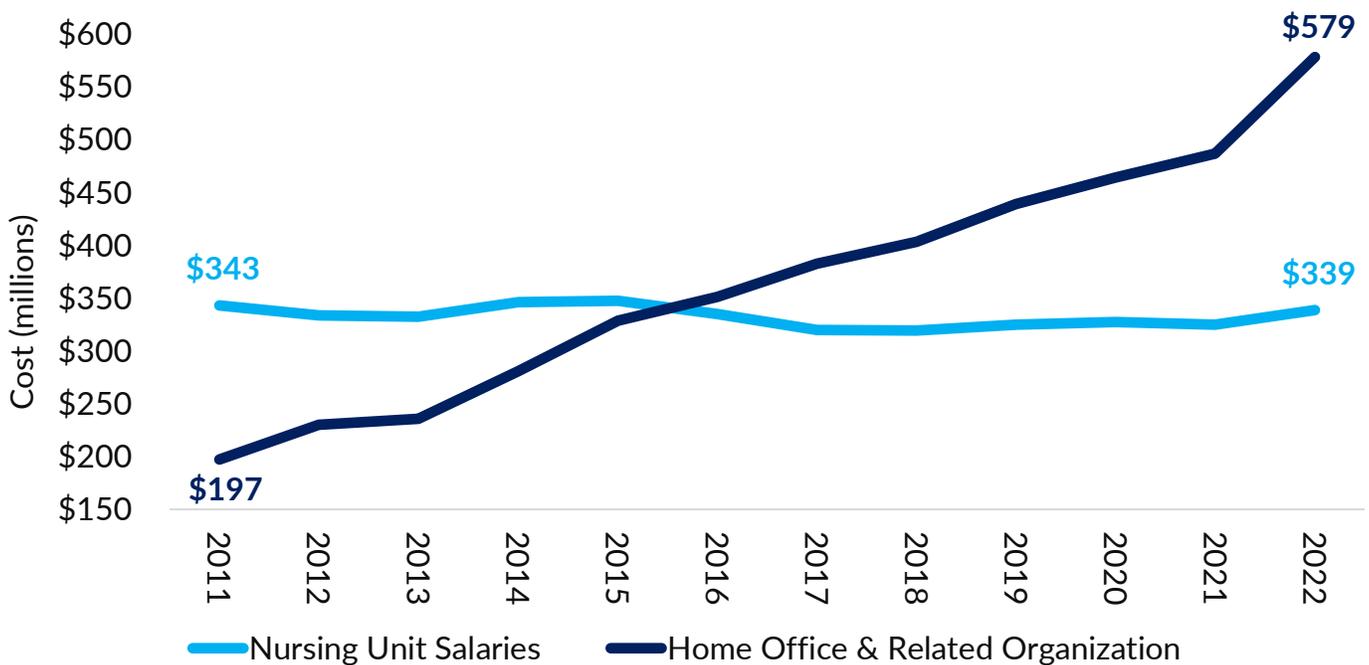
As hospitals’ costs rise, the nation’s healthcare consulting firms have warned that the industry must re-evaluate its business model or risk severe financial hardship. [Oliver Wyman](#), projects that if hospitals are to achieve

financial stability by 2030, they will need to reduce operating costs by 15% to 20%.

Such a warning makes clear that hospitals need new ways to assess their financial health and the direction of their spending. One way is to compare spending priorities over time by comparing the ratio of system costs to general nursing unit salary costs. This metric is important because spending on nursing unit salaries is critical to ensuring high-quality inpatient care particularly since the inpatient hospital of the future is likely to be reserved for those patients who cannot be treated in less-intensive settings.

Among Rhode Island's hospitals, it's possible to see how spending in these two areas changed over 12 years from 2011 through 2022. In 2011, Rhode Island's hospitals spent \$1.74 on nursing unit salaries for every \$1 spent on system costs. By 2022, this ratio was flipped so that only 59 cents was allocated to nursing unit salaries for every \$1 spent on health system costs. (See Exhibit 2.)

Exhibit 2: Health System Expenses Compared with Nursing Unit Salaries
By 2022, only 59 cents was allocated to nursing salaries for every \$1 spent on system costs



Source: [Cost Reports, Centers for Medicare & Medicaid Services](#)

This trend highlights the disproportionate growth in expenses associated with being part of large health systems. Those costs increased an average of 11% annually over the past 12 years, compared with a 3% annual increase in salaries for general nursing units.

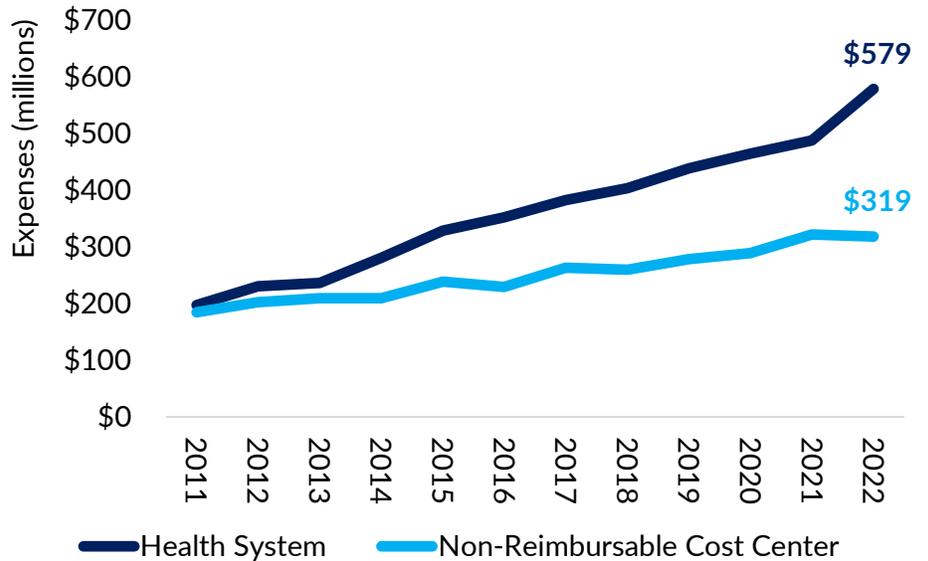
The most recent [Medicare Cost Report](#) shows that among the fastest growing costs at both the national and state levels are the expenses incurred for health system and related organization expenses and non-reimbursable cost centers. (See Exhibit 3.)

In 2022, the combined expenses for health systems in Rhode Island amounted to almost \$600 million. By comparison, the same hospitals spent \$319 million on nursing unit salaries caring for adults and children and for nursing unit salaries in intensive care units and in other care units, including coronary, surgical intensive care, burn care and other special care units listed in the report.

This spending signals a shift in hospital priorities that may compromise the core mission of patient care and likely contributes to the challenges hospitals face in generating operational profit margins. (See Exhibit 3.)

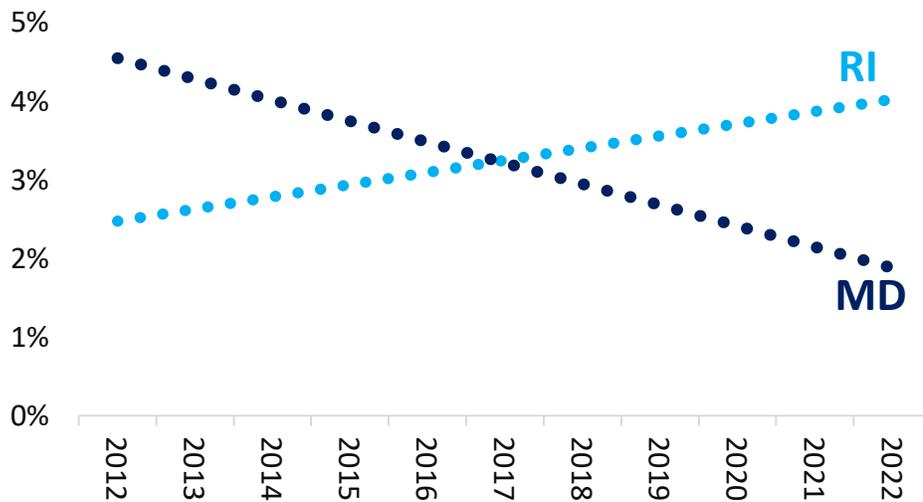
Health policy researchers agree that payment reform is essential to making health insurance more affordable. In response, the federal government has launched the [States Advancing All-Payer Health Equity Approaches and Development \(AHEAD\) Model](#), offering eight states the opportunity to participate in hospital payment reform through all-payer global budgeting.

Exhibit 3: Health System and Non-Reimbursable Costs
A shift in hospital direction that may compromise the core mission of patient care



Source: Cost Reports, Centers for Medicare & Medicaid Services

Exhibit 4: Hospital Overhead Expenses Trend
Over 11 years, MD has used hospital budgeting to curb rising healthcare costs



Source: Cost Reports, Centers for Medicare & Medicaid Services

Rhode Island has applied for one of these slots, seeking to recruit hospitals to implement this model and curb rising healthcare costs. A key example is Maryland, which has been using hospital global budgeting since 2014. Over 11 years, the rate of increase in overhead expenses in Maryland’s hospitals has declined while those expenses in Rhode Island hospitals have continued to rise. (See Exhibit 4.)

The trends in hospital overhead in Maryland versus Rhode Island show the potential benefits of global budgeting as a tool to make healthcare more

affordable and to help hospitals achieve long term financial stability.

The health policy literature is clear: health systems have significantly raised costs, contributing to the financial strain on both hospitals and the broader economy. Zack Cooper, PhD, a Yale health economist, and his colleagues have recently published a National Bureau of Economic Research Working Paper, "[Who Pays for Rising Health Care Prices? Evidence from Hospital Mergers](#)," which provides compelling evidence of the economic impact of rising healthcare prices in the United States. Their study reveals that a 1% increase in healthcare prices, often driven by horizontal hospital mergers, results in a 0.4% reduction in both payroll and employment outside of the health sector, and lowers per capita income by 0.27% at the county level.

Health economists argue that the wide variation in healthcare prices is a clear signal of a market that is not functioning as it should. RIBGH's analysis of rising hospital overhead further underscores this point, indicating that escalating overhead costs amidst increasing price pressures also reflect a dysfunctional market. The evidence is mounting without significant reforms, including a reassessment of hospital business models and the adoption of approaches like all-payer global budgeting, the financial stability of hospitals and the affordability of healthcare will remain in jeopardy.

RIBGH gratefully acknowledges support of its hospital transparency and payment reform initiative from [Arnold Ventures LLC](#), a philanthropy dedicated to tackling some of the most pressing problems in the United States including high health care costs.

Editor's note: This brief on hospital costs is the third in a series analyzing the trends in Rhode Island's hospitals so that health care executives can develop a potential pathway forward to make health insurance more affordable. The first brief, "[Rhode Island's Ongoing Struggle with Rising Health Care Costs](#)," was published in February, and the second brief, "[Hospitals' Rising Overhead Costs Erode Efficiency](#)," was published in June. Both are available at [RIBGH.org](#).