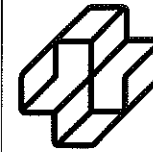


Supply Chain Solutions



hfma™

healthcare financial management association

www.hfma.org/scs

Getting the Most from Your Contracts

By Aaron J. Garmon and Alison B. Flynn

Millions of dollars rest on the decisions made by those who source, negotiate, and manage a healthcare facility's contracts. In most hospitals, this aspect of purchasing belongs to select individuals who possess the expertise to simultaneously maximize vendor performance and minimize potential liabilities.

These are your supply chain professionals, faced with an ever-growing set of responsibilities, and less time to manage them. That said, adherence to a consistent methodology can streamline the contracting process—and result in significant financial rewards.

Adhere to a Contract Approval Process

Both administrators and clinicians must be heard in the contract approval process, as consensus here is a necessity. We advise including the following staff in every review.

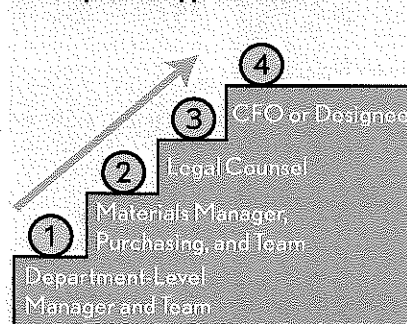
Department-level managers and clinicians.

These front-line authorities possess real insight that can help endorse or debunk a product or service that "looks great on paper." For example, physicians and nurses can help validate claims from medical device manufacturers.

Materials and purchasing staff. Supply chain managers need to review contracts to ensure compliance with the organization's sourcing strategy.

Legal counsel. Attorneys typically review the legal aspects and related liabilities of any business proposition.

Improved Contracting Requires Adhering to the Specified Approval Process



Source: Nexera © 2007. Used with permission

INSIDE THIS ISSUE

Spend Analytics Tool Helps Hospital Alliance Save Millions	4
The Logistics of a Major Logistics Agreement	8
Where Do Distributors Make a Profit?	10
Working with Nurses to Improve Clinical Inventory Management	12

COMING SOON

Managing catastrophic disruptions to the supply chain

Choosing the right GPO

Improving inventory performance

Controlling orthopedic implant costs

The CFO or the CFO's financial designee.

In most organizations, a senior executive, like the CEO or CFO signs off on every binding agreement. In addition, we encourage organizations to define purchasing authorities. At a minimum, the party responsible for the impacted budget line should approve the agreement as well.

When completed, original, signed contracts should reside with the legal department, but other involved groups, such as finance, should retain a copy as well. For reference, copies should be provided to the department head who is expected to work with the vendor. Many times, those working most closely with a vendor are not fully aware of what the vendor may be obligated to provide—whether it's a product, service, or price. Unfortunately, for that reason, hospitals can occasionally miss out on already negotiated opportunities to enhance patient care or lower procurement costs.

Communicate Priorities

With every contract, the goal should be to maximize the net benefit to the organization; by net, we mean the total value of the financial and nonfinancial contributions (for example, the impact on patient safety). Materials managers can easily, and quite unintentionally, stray off course if they don't understand the organization's strategic priorities. For example, a hospital materials manager might implement product conversions to save costs, but such a move could do more harm than good if it results in rattling physicians or risking patient care, all for negligible savings.

Supply chain managers also need to understand some basic information about the organization's financial health. For example, let's say a facility is fortunate enough to have access to significant cash in a low-interest rate environment. If the materials manager knew this, he or she might choose to take advantage of

Many hospitals have standardized contracts that include "must-have" language. Another option is to develop a checklist of key terms and clauses that should be included in every contract. Pilots operate from a checklist; so should materials managers.

certain early payment discounts to save the institution money.

Strive for Consistency in Contracts

Materials managers should review and implement contracts methodically. While individual contracts may vary, certain elements should always be in place. As an example, "out clauses" allow parties, under certain conditions, to disengage from the specified relationship; every contract should have an out. The conditions may include payment of financial penalties, but typically provision of advance notice and purchase of any custom inventories suffice.

Many hospitals have standardized contracts that include "must-have" language. Another option is to develop a checklist of key terms and clauses that should be included in every contract. Pilots operate from a checklist; so should materials managers.

Address All Possible Risks

It's easy for vendors to promise the world, but what happens if they don't come through? Building in the concept of "risk and reward" is one proven approach to handle this situation. For example, let's assume that a vendor touts 99 percent on-time delivery and defines "on-time delivery" in some satisfactory manner. Then, ask the vendor to explain what happens if, in the course of a month or a year (depending on product order volume), the vendor has not kept the promise. The vendor may talk about how third parties verify the numbers or about how the trend could only improve. Remind the vendor that contracts must address the worst-case scenario; then,

find a way to incorporate some penalty for this event. From a legal perspective, any monetary penalty should be no more than the actual loss of time and/or materials the hospital would incur.

Consider the Fine Print

Be certain to run through all of the what-if questions and worst-case scenarios, even

continued on page 14 →

Robert Fromberg <i>Editor in Chief</i>	Robert Neil <i>Editor and Writer</i>
Maggie Van Dyke <i>Project Manager</i>	Kathleen Gallagher <i>Director of Advertising</i>
Ellen Tarantino <i>Advertising Production Specialist</i>	Amy Larsen <i>Graphic Designer</i>

Supply Chain Solutions is published six times a year by the Healthcare Financial Management Association, Two Westbrook Corporate Center, Suite 200, Westchester, IL 60154.

Presorted standard postage paid in Chicago, IL 60607.
©2007 Healthcare Financial Management Association.

Volume 9, Number 3

Subscriptions are \$95 for HFMA members and \$45 for other individuals and organizations. To subscribe, call 1-800-232-HFMA, ext 2. Or visit www.hfma.org/ecs.

To place an ad, contact Kathleen Gallagher at (708) 492-3392 or kgallagher@hfma.org.

Are you interested in contributing an article to **Supply Chain Solutions**? Please e-mail Robert.Neil@Robert@HCFInsights.com.

Material published in **Supply Chain Solutions** is provided solely for the information and education of its readers. HFMA does not endorse the published material or warrant or guarantee its accuracy. The statements and opinions in **Supply Chain Solutions** articles and columns are those of the authors and not those of HFMA. References to commercial manufacturers, vendors, products, or services that may appear in such articles or columns do not constitute endorsements by HFMA.

ISSN 1557-6128

if they seem unlikely or impossible. For instance, what happens if you find a vendor has been overcharging year after year? Will your vendor pay interest to you? Also, thoroughly consider the use of words such as "list price" in the vendor's proposal. What does that actually mean? A list price for what year and from what price book? Are there built-in price escalations? Are new technologies addressed? Is there a credit or exchange clause?

Get a Copy of the Vendor's Contract

Although your hospital may use its own standardized contracts, always ask the vendor representative for what he or she would provide. This way, you can see agreements that the vendor made in the past with your hospital and others. Undoubtedly, over many years, the vendor made alterations in the effort to minimize its own liabilities. Certain contract elements may stand out, and others may simply pique your interest or concern.

Request a Paragraph Review

For more significant contracts, be sure to request a paragraph-by-paragraph review with the vendor. If done by conference call, a pair from materials management can attend, one focused on taking notes and the other on keeping the conversation fluid. Ask the vendor representatives to explain the underlying reason behind questionable clauses. Oftentimes, the representative can provide logic or examples that calm any doubts about the integrity of the vendor, the contract, and perhaps, the representative. You can glean so much more color about the vendor's circumstances and approach from a live discussion. Is this really their "standard" contract, their best deal, their final offer?

Seek a Reasonable Contract Length

Presumably, you chose a high-quality vendor, negotiated fair terms for the contract, and included an out clause (just in case). But be sure to make your effort count.

Depending on the product or service, seek a reasonable term for the duration of the agreement. For hospital products and distribution, three to five years makes sense. However, a special service contract may need only six months. That said, always ask the vendor to include a contract renewal clause that extends the length of the contract upon your request, but never automatically.

Reap Financial Rewards

A centralized contract approval process and a checklist of contract items that address the hospital's strategic direction can significantly improve a facility's chances of developing the best possible contracts—while greatly impacting the organization's bottom line. ☞

Aaron J. Garmong, MBA, is manager for operations with Nexera, a healthcare consulting firm based in New York (garmong@nexeraconsulting.com).

Alison B. Flynn, MHA, CMRP, is vice president for operations and technology with Nexera (flynn@nexeraconsulting.com).

INCREASE YOUR MARGINS In Specialty Services.

No other company increases margins like Goodroe Healthcare Solutions.

Cardiac. Vascular. Orthopedics. Neurosciences. Improving clinical and economic performance in high-cost specialty areas is what we do best. No other company captures as much data at the point of care. No other company can match the integrity of our data. And no other company can measure the overall utilization of products to support clinical quality improvement and cost reduction.

Goodroe is also the only company to receive eight positive opinions by the Office of Inspector General for gainsharing, which is only one of our many models designed to achieve hospital-physician economic alignment. These are just a few of the reasons why we are the industry leader in increasing margins in specialty services. To learn more, call 1-888-226-3001 or email us at ghs@goodroe.com



GOODROE HEALTHCARE SOLUTIONS™
Changing Healthcare

www.goodroe.com

Improve Quality Eliminate Waste Align Physicians Capture Revenue Increase Productivity Assure Compliance