

Testimony
United States Senate Committee on the Judiciary
Hospital Group Purchasing: Has the Market Become More Open to Competition?
July 16, 2003

Mr. Richard Norling
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Subcommittee on Antitrust, Competition, and Business and Consumer Rights
Committee on the Judiciary
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Introduction

Good afternoon, Chairman DeWine, Senator Kohl, and members of the Subcommittee. My name is Richard Norling and I am Chairman and CEO of Premier, Inc. I appreciate having the opportunity to appear once again before this Subcommittee. As you know, Premier Inc. and its group purchasing affiliate, Premier Purchasing Partners, are owned and governed by 198 not-for-profit hospitals and healthcare systems and count as members approximately 1,500 of the leading hospitals in all 50 states, serving some 130 million patients every year.

As stated at last year's hearing, if there is an opportunity to improve, Premier will take it. Last year, we made commitments and I am pleased to tell this Subcommittee today that those commitments were kept. I would also like to take this opportunity to point out the valuable contributions that Premier continues to make to our owner and member hospitals, and to the communities and patients they serve as well as to the broader healthcare marketplace.

Proactive Steps Taken

In response to your challenge to improve business practices at Premier and throughout the industry, we supported the Health Industry Group Purchasing Association (HIGPA) in its adoption of an industry-wide code of conduct. This Industry Code provides key guidelines for conduct in major areas including conflict of interest and contracting practices.

But we went farther when, in August 2002, we adopted 13 additional principles that raised the bar even higher and addressed several important contracting and fee-related issues that the Industry Code could not address.

In October, we took an additional and very important step with Premier's adoption of the Hanson report and its 50 recommended best ethical practices for GPOs. This was the groundbreaking work of Professor Kirk Hanson, Executive Director of the Markkula Center for Applied Ethics at Santa Clara University in California and distinguished business ethicist. By embracing the Hanson report and its recommendations, we have provided assurance of our commitment to the highest ethical standards in order to respond to the concerns of this Subcommittee and other interested parties. At the same time, we believe strongly that these principles make sound business and strategic sense for Premier, other GPOs and the other participants in the healthcare marketplace.

With the adoption and implementation of our Code of Conduct:

- We contract for physician preference products on a multi-source basis with no GPO commitment levels or “bundling” with unrelated products. For example, in the last year, we re-bid pulse oximetry products – which had been raised as an area of concern at your previous hearing. We sent out requests for proposals to all suppliers in this area. We reviewed these submissions and contracted with three different manufacturers. These contracts contain no GPO commitment levels and no bundling with unrelated products.

Another good example is our contracting for medical-surgical products that hospitals use in neurosurgery. Previously, these products were all grouped in one contract area. With our hospital members’ input, we broke these products into eleven separate product categories and put all eleven out for bid on a multi-source, unbundled basis without GPO commitment levels. As a result, we added two new suppliers in this area, including Integra NeuroSciences, a small innovative manufacturer of implants, instruments and monitors used in neurosurgery and intensive care units.

- We substantially revised and improved our Technology Assessment and Technology Breakthroughs programs to further assure that they operate in a fair, timely, confidential and unbiased manner. We placed these programs under the direction of Jack Cox, M.D., and supplemented our assessment activities by outsourcing functions to several highly qualified external firms. Those firms include:

- the Health Technology Center (a non-profit research and education organization that provides strategic information and resources);
- the Institute of the Future (a non-profit research firm specializing in long-term forecasting);
- SG-2 (a firm that identifies and analyzes changes in the technology and business of health care); and
- ECRI (formerly the Emergency Care Research Institute, a health services research agency).

In addition, we entered into an agreement with ECRI to support our assessment for our Technology Breakthroughs program. ECRI, a not-for-profit health services research agency, has a sterling reputation in this field and is adding much to our efforts to bring innovative products to our members. Further, we worked to reduce the cycle time of Technology Breakthroughs reviews. In the early days of this program, reviews took longer than any of us would have liked – not surprising in a new effort. But substantial improvements have been made. We have gone from a review process of more than eight months to one that takes only four months from the time Premier receives a completed application to the time a recommendation is made.

- We incorporated our Code into our policies and procedures, including our conflict of interest policies. Every single employee and advisory committee member received training on the Code and our updated policies, and each has certified compliance. Further, we have applied our conflict standards to all employees, not just those directly involved in contracting, and prohibited all employees from holding equity stakes in any participating vendors.

- We continue to limit administrative fees to 3%, and our average fee is 2.1%. We do not charge “upfront” fees or marketing fees, and we do not accept administrative fees in the form of vendor equity or require vendor participation in any additional services for which fees may be charged. In addition, we have begun the process of standardizing administrative fees for each bid process and product category. This major innovation was recommended by Professor Hanson to eliminate the potential or perception that fees or fee levels impact product selection.

- We continued our practice of not private-labeling products.
- We contract for 3 years or less, with limited exceptions.
- We continue to seek out small and woman- and minority-owned suppliers for contracts. At present, approximately 30% of our suppliers are small companies as defined by the Small Business Administration and a number of these companies are also woman- and minority-owned businesses.
- We continue to focus on environmental issues, an effort which was recently recognized when the Hospitals for a Healthy Environment, H2E, awarded Premier the Champion for Change Award for our efforts to contract for the most environmentally safe products.
- At the close of this calendar year, our Ethics and Compliance officer will make publicly available a report on Premier's compliance with our Code. This report will be in addition to the Certification of Industry Code Compliance that we made earlier this year.

When we introduced our Code, Senators DeWine and Kohl called it "the most significant reform to the hospital purchasing system since the development of...group purchasing...." On other occasions, Senator Kohl was kind enough to describe our efforts as setting the "gold standard" for the industry and to cite us as "the industry leader." We are greatly encouraged by the response to our Code and are committed to working with you and the other members of the Subcommittee in a good faith and productive way to continue to improve our industry and healthcare in America.

The Value of Premier

Premier is a healthcare alliance that is owned by non-profit hospitals and healthcare systems. Our core purpose is to improve the health of communities by helping our members improve quality and cost effectiveness. Group purchasing is a vitally important part of that purpose, but it is only one of several cornerstones of a broader strategy to support our owners' and members' efforts to improve their performance. Others include an ongoing effort to help improve the quality of care by using the wealth of comparative data on clinical performance Premier has accumulated, and by enhancing our capabilities to manage hospitals' enormously complex supply chain processes and assess new and existing technologies. We also provide insurance and risk management services that enable our member hospitals to better manage the major risks inherent our industry. I would like to bring you up to date on key successes in these cornerstones of Premier's operations.

Since I testified before this Subcommittee in April 2002, Premier has continued to be highly successful in helping its hospital members control costs. One of our most notable achievements in this effort has been the adoption of a strategy known as strategic sourcing.

At its basic level, following this strategy allows suppliers with products that are focused in specific product categories to compete with suppliers that offer a broader line of offerings. A terrific example of this strategy in action is in custom sterile procedure trays (these are trays of medical/surgical supplies customized for a particular procedure) where we moved from a sole-source award to contracts with four suppliers including one woman-owned company. Our owners and members benefit from this strategy because it introduces additional competition into categories that would otherwise be dominated by a major supplier, and our entire healthcare system benefits because it fosters greater competition within vital supply categories.

As part of our strategic sourcing effort, we have also adopted advanced tools that allow us to conduct

reverse auctions for certain types of products. This approach has proven successful in other industries, and Premier is leading the effort to utilize this approach within the healthcare industry. We started using this technology in the last year, and have now completed auctions for 16 product categories representing \$434.5 million of historical spending, and have achieved a total savings opportunity of over \$103.5 million vs. our previously contracted pricing. In fact, this tool has been so rewarding that we are currently working to implement the reverse auctions in ten additional categories over the course of the next several weeks.

Examples of cost savings opportunities we have achieved through the use of reverse auctions include:

- Amiodarone (pharmaceutical) – 61.7%
- Patient Aids – 35.3%
- Waterless Hand Gels and Solutions – 33%
- Vital Sign Monitors/Cuffs – 30.6%
- Surgeon Gloves – 30%
- Salad Dressing & Sauces – 26.4%
- Soaps and Lotions – 26%
- Lap Sponges and OR Towels – 26%
- Textiles and Textile Services – 25.2%
- Exam Gloves – 25%
- Standard Surgical Set-up Kits and OR Access – 24%
- Personal Protective Apparel – 21.0%
- Disposable Anesthesia – 14%
- Surgical Hand Scrubs – 11%
- Patient Warming – 5%
- Wound Drainage - 3%

Widening the focus to GPOs as a whole, over the past year, the evidence of the tremendous value we deliver to hospitals and their patients has continued to build. In one major study conducted by Muse & Associates for HIGPA and released in October 2002, healthcare institutions reported that they saved from 10% to 15% of their non-labor costs by channeling their purchases through GPOs. That translates into savings for the U.S. healthcare system in 2002 of between \$19.0 billion and \$33.7 billion each year.

According to a May 2003 study by The Lewin Group, GPOs save their member institutions an average of 10.4% of their total supply costs. Savings of this magnitude are critical to the ability of many hospitals to confront the powerful squeeze between increasingly restrictive insurance reimbursement and the challenge of uninsured patients on the one hand, and rising labor and supply costs on the other. Of course, hospitals experience enormous cost pressures and can, therefore, benefit significantly by each dollar saved. For not-for-profit hospitals, the money saved can be dedicated to help cover the medical costs of the under- and uninsured, augment stretched hospital staffs, increase bioterrorism readiness and/or pay for costly medical liability insurance.

Controlling the costs of supplies is an area in which hospitals can make a significant difference. If GPOs were to operate within a significantly more restrictive business model, these savings might be drastically cut to the detriment of hospitals and their patients. According to Muse & Associates, under a more restrictive model, public and private expenditures for healthcare services and supplies would increase by approximately \$2 billion, and that's with only a 1% increase in the cost of medical supplies. That would mean more than \$1 billion in higher costs to the Medicare and Medicaid programs alone.

It is clear that, for many hospitals, GPOs like Premier Purchasing Partners are much more than a convenience or a tool of purchasing management. The economies of scale they provide play a crucial role in sustaining vital medical services. A significant drop in those savings could have devastating effects – especially for the not-for-profit hospitals that own Premier. Still, even with the benefit accrued from our cost control measures, we have witnessed an acceleration of healthcare costs in several areas that should be of great concern to all those present here today.

Turning to Premier's role as a performance-improvement organization, we help our hospitals undertake initiatives to improve clinical performance and supply chain value by using the vast reservoir of collected knowledge and experience contained within our databases. Drawing on the experience of thousands of healthcare professionals in hundreds of hospitals, Premier's databases are among the most comprehensive and accurate sources of clinical, financial and operational metrics available anywhere. Through our Healthcare Informatics programs, member and non-member hospitals are able to apply detailed, comparative data and performance-improvement expertise in their continuing efforts to improve quality.

Premier hospitals continue to achieve important performance improvements through initiatives assisted by Premier data in a wide range of clinical treatment areas, including acute myocardial infarction, congestive heart failure, coronary bypass grafts, community acquired pneumonia, hip- and knee-replacement, spinal surgery, pregnancy and related conditions, and stroke.

We are especially pleased that the federal Centers for Medicare and Medicaid Services (CMS) has chosen our database system, Perspective, as the foundation of a three-year demonstration project to recognize and reward high-performing hospitals through increased reimbursements. As you know, this effort is a key step toward putting the weight of the major federal health insurance programs behind the growing movement toward encouraging quality of care. The hospitals across the nation that will voluntarily participate in this pilot program are being drawn from among the approximately 525 hospitals that already participate in the Perspective program. By submitting clinical and financial data to Premier, we generate regular clinical performance reports that the hospitals will use in their own planning for improvement. This data will provide the basis for Medicare to reward hospitals that provide the highest quality of care with higher reimbursements and will pave the way for a wider national effort to enable healthcare providers and payers to work together on an agenda of healthcare quality.

Several Premier members committed publicly to the project on the first day – among them Aurora Health Care of Wisconsin and Kettering Medical Center of Kettering, Ohio – and we were pleased that Kettering CEO Frank Perez was able to participate in the July 10, 2003 news conference in Washington, D.C. announcing this program. In addition, according to the July 10 Milwaukee Journal Sentinel, Aurora President Ed Howe said that the idea behind the experiment is that hospitals with better quality should be able to save the government “significant amounts of money.”

Another important service we provide to our not-for-profit hospitals, unrelated to group purchasing, is insurance. Through Premier Insurance Management Services (PIMS), we help hospitals manage their insurance costs while improving risk management and claims capabilities. In these days of skyrocketing insurance costs to cover the risks inherent in delivering healthcare services, liability coverage can be very expensive or even difficult to obtain in many areas. Working with PIMS, hospitals have come together to create insurance pools (that they own) to reduce cost, manage risk and improve clinical performance. PIMS is able to help hospitals share information on best practices and network solutions. Increasingly, we hope to be able to use the tremendous power of Premier's clinical databases to analyze the relationships between insurance claims and clinical outcomes. Our goal is to help hospitals focus on risk prevention, so they can improve outcomes for patients and bring

down the costs of insurance claims simultaneously.

In addition to lowering costs for all our members, we have paid attention to special needs by setting up, on behalf of our more than 60 children's hospitals, dedicated committees that specialize in evaluating and contracting for pediatric medical products.

To sum up Premier's value, our contribution to hospitals' efforts to control costs through group purchasing contracts alone is a substantial one; without it, many not-for-profit hospitals would have no choice but to make significant cuts in staffing or services. But the value we contribute as a performance-improvement organization to the quality and effectiveness of Premier hospitals and the nation's healthcare system is also very significant and we will continue to look for new and exciting ways to provide meaningful value.

Conclusion

Premier has long proved its value to the healthcare system and continues to play a critical role in helping hospitals keep costs down and maintain the quality of healthcare. We at Premier have rolled-up our sleeves and plunged into the job of creating a set of practices and principles that will ensure the highest standards of ethical conduct. We made a strong commitment to set the pace of leadership for our industry. We lived up to that commitment by adopting the tough, comprehensive principles embodied in the Industry Code, the Premier additional principles, and the recommendations included in the Hanson report.

While I want to emphasize that you can count on our continuing cooperation and support, we believe that the time is right to encourage others to do their part in an ongoing effort to ensure the quality and effectiveness of our nation's healthcare system.

Everyone involved in the healthcare system in this country should be working towards the same mission: to provide the best quality care and access to that care for every individual. Organizations such as Premier play a valuable but discrete role in the healthcare system. Going forward, we must ensure that every participant in healthcare commits to the highest standards. At Premier, we are committed to doing our part.

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