Improving Urgent Care Center Profitability Through Medical Supply Management and Accounting

Urgent message: Many urgent care centers lack an inventory management process and do not accurately account for their utilization of supplies. Improving how a center manages and accounts for supplies can have a direct impact on the bottom line.

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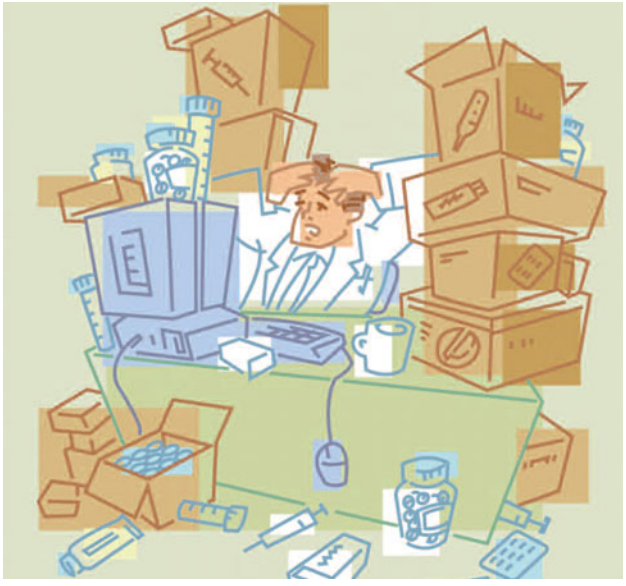
Introduction

A quick and easy way to improve your urgent care center's profitability may be as close as your supply closet. Many urgent care centers lack defined processes for managing and replenishing medical supplies and their financial statements fail to accurately capture supply inventories and match supply utilization to patient revenues. This results in buying the wrong types of supplies, buying too many supplies, losing supplies to inventory shrinkage, overstating supply expense on the income statement, and understating the value of supplies as an asset on the balance sheet.

Issues With Medical Supply Management in Urgent Care

Medical supplies are items like Band-Aids, syringes, antiseptic, casting material and gauze that are "substantially consumed" or "materially altered" when used in patient care. In urgent care centers, supplies generally consist of consumables (including injectables and other pharmaceuticals) but they can also include small tools and minor equipment (**Table 1**).



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Some individual supplies (such as suture kits and splints) can be quite costly, but rarely do supplies account for a significant portion of a center's total

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Table 1. Accounting for Minor Equipment

Although most of what constitutes "medical supplies" in an urgent care setting are consumables used in patient care, there are a number of handheld diagnostic tools that have costs below the threshold of a depreciable asset. Examples include electronic thermometers, scopes, and blood pressure cuffs. Instead of carrying these items on the balance sheet as a long-term asset and expensing depreciation—as is done for furnishings, fixtures, and equipment—minor equipment is typically expensed as purchased. These items should be assigned to rooms and checked daily to prevent loss.

Table 2. Common Internal Control Weaknesses and Strategies to Improve Controls Related to Medical Supply Inventories

Common Internal Control Weaknesses	Strategies to Improve Control
• Lack of a consensus formulary—duplicative or redundant SKUs are carried in inventory. • Lack of utilization statistics—center administrators do not track how frequently items are used or replenished. • Lack of visibility of current inventory—supplies are expensed as ordered, meaning the value of supplies is not accurately depicted as a center asset. • Lack of minimum on-hand or "trigger" re-order quantities—ordering occurs when items "appear" low or are close to running out with little data to support the decision. • Lack of purchase approval processes—purchase orders are processed without management review. • Lack of physical controls—supplies are stored in locations throughout the center versus one central, lockable supply closet.	• Engage physicians, nurses and administrators in developing a "formulary" to help eliminate duplicative SKUs and identify cheaper or more desirable alternative products when available. • Interview staff and "walk through" the existing order system and identify weaknesses and procedures that are particularly time consuming. • Implement a structured inventory management process or system to track supplies on hand and used in patient care, and to facilitate re-orders. Use system reports to create accounting entries. • Review all the locations that are used for storage. Keep unopened supplies in a central, locked closet and sign out to specific storage areas or to individual patients if billable.

expenses. Supplies used are much less extensive than in, say, surgical centers, because most urgent care visits are for low-acuity infections, cold/flu, skin conditions, allergies, etc. Perhaps because medical supplies are viewed as "incidental" to treating patients and are not a major expense category like salaries and rent, many urgent care centers simply "write-off" supplies without further consideration.

Supply Management Starts With a Consensus Formulary

In referring to medical supplies, a stock-keeping unit (SKU) refers to a unique item. In your kitchen cupboard, for instance, "oatmeal" may constitute a single "product" but in a supermarket, each distinct brand, flavor, and box size constitutes a separate "SKU." This grocery analogy is relevant because—just as any cereal on the shelf may satisfy your morning hunger—your urgent care center likely carries multiple SKUs that serve the same clinical purpose. Without an agreed-upon supply "formulary," if Provider A wants one brand of suture kit and Provider B (who only works weekends) wants a different brand, it's common for a center to stock both SKUs to appease both providers.

If all of a center's providers can agree on one SKU for each clinical function—giving fair consideration to quality and price—the number of SKUs ordered and stored by the center can be reduced. In addition, by concentrating all orders for a product into one SKU, the center can better take advantage of quantity discounts. To prevent providers and others in the center from ordering whatever they want or need on a whim, however, a formal policy should require that additions or deviations from the formulary be approved by the center's medical director.

The Need for Formal Supply Management Processes

Even when there's a consensus formulary, many centers lack formal supply management processes to ensure that the "right" quantities of supplies are always on hand. When administrators cannot track how frequently items are used or replenished, they tend to place orders when inventories "appear low" or actually run out. But because running out of a critical supply can impair patient care, it's likely the center administrator orders and stores far greater quantities than would normally be used in the subsequent weeks or months.

Given that major medical supply houses such as McKesson, PSS World Medical, and Henry Schein offer

service level agreements ensuring 48- to 72-hour delivery of nearly any item in their catalogs, a center really has no need to carry more than a couple weeks' worth of supplies at any given time. Larger inventories increase the risk of shrinkage as supplies expire, spoil, become damaged, or are pilfered. And when these excess quantities start to crowd central storage spaces, supplies end up in exam room cabinets, provider station drawers, and other locations throughout the center—further obscuring visibility as to what supplies are on hand.

Electronic Supply Management Systems

A variety of Web-based, supplier-provided and standalone inventory management systems have been designed for medical practices can be implemented in an urgent care center. These systems expand upon the use of the SKU identifier to:

- Track current inventory levels against the formulary;
- Track the date supplies were received, number of days on hand, and days until expiration;
- Track supply utilization by category, type, SKU and lot;
- Charge supplies to specific patients, clients or business units;
- Identify minimum on-hand and trigger reorder quantities;
- Create, track and process requisitions and purchase orders;
- Integrate with supply vendors for electronic ordering and auto-replenishment;
- Reconcile accounts payable invoices to purchase orders and receipts; and
- Create inventory reports to facilitate physical counting.

Electronic inventory systems are most effective when integrated with bar code technology. Using a handheld device, staff "scans" the bar codes on individual items as they're consumed in patient care (or on boxes as

Table 3. Comparison of Accounting Methods for Medical Supplies in Urgent Care

Accounting Method Used by Many Centers: Expense Supplies as Used	Hybrid Method: Expense Supplies as Used but True-up Balance Sheet	Generally Accepted Accounting Principles: Accurate Valuation of Supplies on Balance Sheet
• Initial Value of Supplies Not Carried as a Balance Sheet Asset • Purchase Supplies: Debit the Expense Account • Utilize Supplies: No Entry • No Ending Supply Inventory Occurs	• Starting Asset: Initial Value of Supplies • Purchase Supplies: Debit the Expense Account • Utilize Supplies: No Entry • Year-end Inventory: True-Up the Asset Account; Debit or Credit the Expense Account	• Starting Asset: Initial Value of Supplies • Purchase Supplies: Debit the Asset Account • Utilize Supplies: Credit the Asset Account Debit the Expense Account • Monthly or Quarterly Inventory: True-Up the Asset Account Debit or Credit the Expense Account
Benefits: • Easy—all supplies are expensed as purchased; does not require an inventory management system • Overstating supplies expense may reduce taxable income	Benefits: • Considers the value of supplies held as a center asset	Benefits: • More accurately reflects value of supplies held as a center asset • More accurately reflects the cost of supplies (used to serve patients) during a particular period
Drawbacks: • Typically undervalues the asset of supplies on hand • Typically overstates the cost of supplies used in patient care • Can trigger IRS audit for overstatement of supplies expense	Drawbacks: • Supplies expense can vary significantly based on timing of purchases • Supplies expense is not reflective of supply utilization associated with patient revenue	Drawbacks: • Requires greater effort in managing supply inventories, which can be aided by technology and process improvements

they're opened or removed from the storage closet[i]). The system then electronically updates inventory records, facilitating on-demand reports of supplies on hand and those used during a reporting period. Periodic inventory can be facilitated using the bar code scanner and system reports. The system can even indicate when quantities fall to preset "reorder" levels. More sophisticated systems can automatically create a purchase order and submit an electronic order to the supply vendor for fulfillment.

Not all urgent care centers will want to computerize their ordering and inventory management processes. But applying simple internal control procedures and routine authorizations for expenditures will still significantly help in managing supply costs. When an inventory system is implemented, quantities in use and on hand tend to be consistent and, therefore, accurate records lead to generation of a more consistent month-over-month supply expense on the income statement; reduction in overstock, waste and spoilage; and more efficient use of storage space.

i. Accounting rules generally consider a box containing multiple items to be "consumed" and "no longer in storage" once the box is opened. At this point the entire contents of the box should be expensed.

Account for Supply Utilization

From an accounting standpoint, an urgent care center's management is responsible for the accurate presentation of financial statements prepared for use by creditors and investors under Generally Accepted Accounting Principles (GAAP). Accurately representing Supply Expense on the Income Statement and the value of Supply Inventory on the Balance Sheet requires adequate financial controls, as illustrated in **Table 2**.

Often urgent care centers do not maintain accurate supply inventories on their books because they expense all supplies at the time of purchase. The issue with this—illustrated by **Table 3**—is that an asset worth up to $50,000 (in aggregate) is hidden away in cabinets, drawers, and under sinks while the Balance Sheet

"Many urgent care centers simply 'write-off' supplies without further consideration."

understates the value of owners' equity in the business.

Moreover, the common practice of expensing all supplies upon purchase violates accounting principles that call for revenue and expenses to be matched during the same period each is incurred. In any given month that a large supply order is processed, supplies expense as a percent of patient revenue may climb, leading to incorrect conclusions being drawn from the income statement. Likewise, a center could improve its profitability in a given month by just not placing any supply orders.

As illustrated in **Table 3**, center accounting for supplies could be improved by carrying a beginning supply inventory on the balance sheet, continuing to expense supplies as used, and doing a periodic "true-up" based on a physical inventory count. But the best alternative is to record purchases in the inventory (asset) account and make a periodic journal entry (weekly or monthly) to expense supplies that are used. The availability of data from an inventory management system facilitates this routine. In addition, a physical inventory will be matched to the account balances and any differences analyzed. With supply expense more reflective of utilization, a center operator can more effectively identify trends, including changes in supply costs.

Payor Reimbursement for Medical Supplies

In general, urgent care centers are not specifically reimbursed for supplies used in the ordinary treatment of patients. This is particularly true when a center has contracts that pay a "flat fee" or "global rate" per visit. But some fee-for-service contracts do reimburse some supplies—particularly supplies used in procedures like casting and suturing. Thus, center administrators should understand which supplies are reimbursed by which payors using which codes. When supplies are reimbursable, a process should be in place to accurately capture supply utilization on the patient's charge ticket. Providers, medical assistants, and charge entry staff also need to be educated as to which payors reimburse which supplies to ensure chart documentation such that the center receives its full reimbursement.

Conclusion

Improving your urgent care center's medical supply management processes can have a direct impact on its financials by better tying supply utilization expense to patient revenue and by better reflecting supplies on hand as an asset of the center. Effective supply management in urgent care entails establishing a formulary, implementing processes related to the storage and replenishment of supplies, capturing supply utilization and shrink, and establishing proper accounting practices. ■