Road to Value: What’s the Financial Strategy to Survive the Transition to New Payment and Care Delivery Models

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Road To Value Agenda

- Why the Need to Prepare for Transition
- Top 10 Indicators to be Monitored and Managed
- How to Monitor
- Importance of Strong Indicators
- Documenting Value
- Key Strategy Overview
Why the Need to Prepare for Transition

• The historic growth in health care spending is not sustainable

• New payment models have been proposed and are at different stages of implementation

• Patients and payors are demanding a change
  • Access to data is providing them the tools they need to make decisions to force the change
Why the Need to Prepare for Transition

- This slide shows the growth in health care spending from 7% of GDP in 1970 to 17% in 2013.

Why the Need to Prepare for Transition

- These factors will require providers to move from a model that focuses on volumes to one that focuses on value.

- Value = Quality / Cost
Strategies for Transitioning

• The road to value will be a bumpy one as payors change their payment models and incentives as different rates and in different models

• The uncertainty caused by the variances in timing and approach requires providers strengthen their financial position today
Strategies for Transitioning

• Improve Financial Indicators
  • Improve ability to sustain financial performance in the future
  • Develop financial reserves to assist organization during the transition period
10 Indicators to be Monitored and Managed

• These indicators should be monitored during the preparation for the transition as well as the post transition period

• Critical Access Hospital 2012 Financial Leadership Summit
  • 15 participants
  • Identified top 10 indicators
10 Indicators to be Monitored and Managed

- There are more indicators available, but these are those that have been determined to be most valuable

- Other indicators may be used to help provide additional analysis in areas for which a problem has been identified
Top 10 Financial Indicators

- Days in Net Accounts Receivable
- Days in Gross Accounts Receivable
- Days Cash on Hand
- Total Margin
- Operating Margin
- Debt Service Coverage Ratio
- Salaries to Net Patient Revenue
- Payor Mix Percentage
- Average Age of Plant
- Long Term Debt to Capitalization
Days in Net Accounts Receivable

• **Definition**
  - Measures the number of days it takes an organization to collect its payments

• **Calculation**
  - Net Patient Accounts Receivable / (Net Patient Revenue / 365)

• Favorable values are below the median

• 2012 CAH U.S. Median = 52.74 days

• **Causes for unfavorable values**
  - Inadequate registration and collection processes
  - Poor communication
  - Chargemaster problems
Days in Gross Accounts Receivable

• Definition
  • Measures the number of days it takes an organization to collect its payments. Over time should be comparable to Days in Net Accounts Receivable.

• Calculation
  • Gross Patient Accounts Receivable / (Gross Patient Revenue / 365)

• Favorable values are below the median

• 2012 CAH U.S. Median = 52.74 days

• Causes for unfavorable values
  • Inadequate registration and collection processes
  • Poor communication
  • Chargemaster problems
Days Cash on Hand

• Definition
  • Measures the number of days an organization could operate if not additional cash was collected or received

• Calculation
  • \[
  \frac{(\text{Cash} + \text{Investments})}{((\text{Operating Expenses} - \text{Depreciation} - \text{Bad Debt}^*) / 365)}
  \]
  • * Only include Bad Debt if included in Operating Expense

• Favorable values are above the median

• 2012 CAH U.S. Median = 69.07 days

• Causes for unfavorable values
  • Poor profitability
  • Excess Days in Accounts Receivable
Total Margin

• **Definition**
  - Measures the control of expenses relative to revenues

• **Calculation**
  - Excess Revenues over Expenses / Total Revenues * 100

• **Favorable values are above the median**

• **2012 CAH U.S. Median = 2.61%**

• **Causes for unfavorable values**
  - High expenses
  - Lack of public financial support
Operating Margin

• Definition
  • Measures the control of operating expenses relative to operating revenues

• Calculation
  • Net Operating Income / Total Operating Income * 100

• Favorable values are above the median

• 2012 CAH U.S. Median = 1.13%

• Causes for unfavorable values
  • High expenses
Debt Service Coverage Ratio

• Definition
  • Measures the control of operating expenses relative to operating revenues

• Calculation
  • Net Operating Income / Total Operating Income * 100

• Favorable values are above the median

• 2012 CAH U.S. Median = 1.13%

• Causes for unfavorable values
  • High expenses
Salaries to Net Patient Revenue

• Definition
  • Measures labor costs relative to the generation of operating revenue from patient care

• Calculation
  • Salaries / Net Patient Revenue

• Favorable values are below the median

• 2012 CAH U.S. Median = 44.87%

• Causes for unfavorable values
  • Poor productivity
Payor Mix Percentage

• Definition
  • Measures proportion of patients represented by each payor type

• Calculation
  • Inpatient = Inpatient Days for Payer / (Total Inpatient Days – Nursery Days – Nursing Facility Swing Bed Days)
  • Outpatient = Outpatient Charges for Payor / Total Outpatient Charges

• Favorable values are below the median

• 2012 CAH U.S. Median for Medicare Inpatient = 73.59%

• Causes for unfavorable values
  • Failure to market and capture non-Medicare patients
Average Age of Plant

• Definition
  • Measures average age in years of the buildings and equipment of an organization

• Calculation
  • Accumulated Depreciation / Depreciation Expense

• Favorable values are below the median

• 2012 CAH U.S. Median = 9.83 years
Long Term Debt to Capitalization

• Definition
  • Measures the percentage of net assets that is debt

• Calculation
  • Long Term Capital Liabilities / Net Assets

• Favorable values are below the median

• 2012 CAH U.S. Median = 17.26%
Why now? – Why in the future?

- These indicators provide a good comparison for
  - Profitability
    - Total Margin
    - Operating Margin
  - Liquidity
    - Days Cash on Hand
    - Days Revenue in Gross Accounts Receivable
    - Days Revenue in Net Accounts Receivable
  - Capital Structure
    - Debt Service Coverage
    - Long Term Debt to Capitalization
  - Revenues
    - Payor Mix Percentage
  - Cost
    - Salaries to Net Patient Revenue
    - Average Age of Plant
Why now? – Why in the future?

• Importance today
  • Demonstrates ability to manage overall performance of organization
  • Strong indicators will assist in accumulating required resources to endure the challenges during the transition
    • Inconsistent incentives
    • Payor transitions / billing rules
Why now? – Why in the future?

• Importance tomorrow
  • Anticipation that financial challenges will only increase
    • Long term survival depends on the ability to manage these indicators
  • Allows for early detection of downward trends
• Goal
  • To perform at a level better than the national, region, and state average
  • Remember the average facility is struggling
How to Monitor

- Monitor all 10
  - Monthly
  - Quarterly
  - Annually

- Comparison
  - State
  - National
How to Monitor

• **Values**
  - Monitor trends as well as absolute values
  - Trends can be early indicators of potential problems

• **Initiate action**
  - It is more than just monitoring that is important
  - What changes are being made to address weak indicators or downward trends?
  - What accountability has been assigned in the organization
Importance of Strong Indicators

• Strong indicators will put the provider in a leading position moving forward
  • Strong indicators over time lead to improved reserves and the ability to “weather the storm” during challenging times
  • The transition from volume to value will require most providers to establish new relationships with other providers (affiliations, alliances, acquisitions, mergers, etc.)
    • Weak financial indicators may increase challenge to find interested parties or leave provider on their own
Importance of Strong Indicators

- Strong indicators will put the provider in a leading position moving forward
  - Past performance is an indicator of future performance
  - Promises of improvement/strength in the future are hard to sell is past performance does not support ability to perform at that level
  - Potential partners do not have the cash reserves to support weaker organizations in the same manner as the past
Documenting Value

- Strong financial indicators will help provide the necessary resources to transition from volumes to value
- Documenting value will help provide the necessary information to attract patients, payors, and strategic partners
Documenting Value

- Important to monitor and manage value indicators before Medicare and others announce payment programs around value
  - Historical data will be used in initial payment models
  - Initiating change in reported value takes time
Value under PPS – Value Based Purchasing (VBP)

- Adjusts payments to hospitals under the IPPS based on the quality of care they furnish to patients
  - Clinical process of care (timing of tests, interventions, orders, test results)
  - Patient experience of care (HCAHPS)
  - Outcome – (hospital mortality measures for acute MI, heart failure, pneumonia, the central line associated bloodstream infection)
  - Efficiency – (Medicare spending per beneficiary)
- Zero sum game for CMS, winners and losers!
VBP Domain Weightings

- Weightings begin with focus on Clinical Process of Care and Patient Experience and transition to focus on Patient Experience, Outcomes, and Efficiency.
VBP Reductions to Providers

- Reductions begin with 1.00% in FY 2013 and increase each year up to 2.00% in FY 2017
Value under PPS – Value Based Purchasing (VBP)

• Anticipate that this payment model will be transitioned to Critical Access Hospitals
  • Could be an adjustment to 101% cost based reimbursement
  • Would most likely utilize quality data that already exists
Value under PPS – Value Based Purchasing (VBP)

• Ability to manage quality indicators
  • Protects against potential future payment reductions
    • Reduce the learning curve
  • Demonstrates value
    • Patients
    • Payors
    • Potential partners
Key Strategies Overview

• Identify and monitor the 10 financial indicators
• Report and monitor key quality indicators
• Successful providers will be able to improve their ability to remain financial stable during the transition from volume to value
Questions?

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