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

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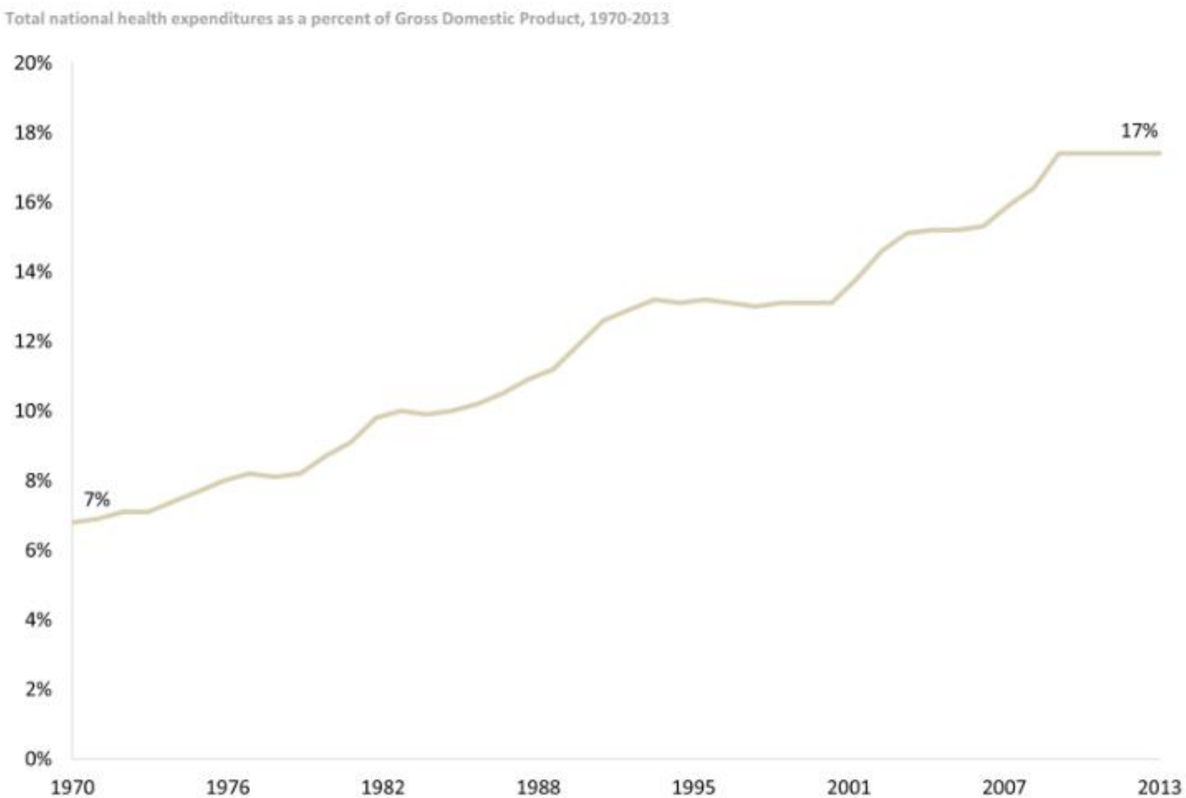
Road To Value Agenda

- Why the Need to Prepare for Transition
- Top 10 Indicators to be Monitored and Managed
- Why Now? – Why in the Future?
- 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



Source: National Health Expenditure (NHE) data from Centers for Medicare and Medicaid Services, Office of the Actuary, National Health Statistics Group

Peterson-Kaiser Health System Tracker

- This slide shows the grow 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
  - (Cash + Investments) / ((Operating Expenses – Depreciation – 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

Why now? – Why in the future?

- 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

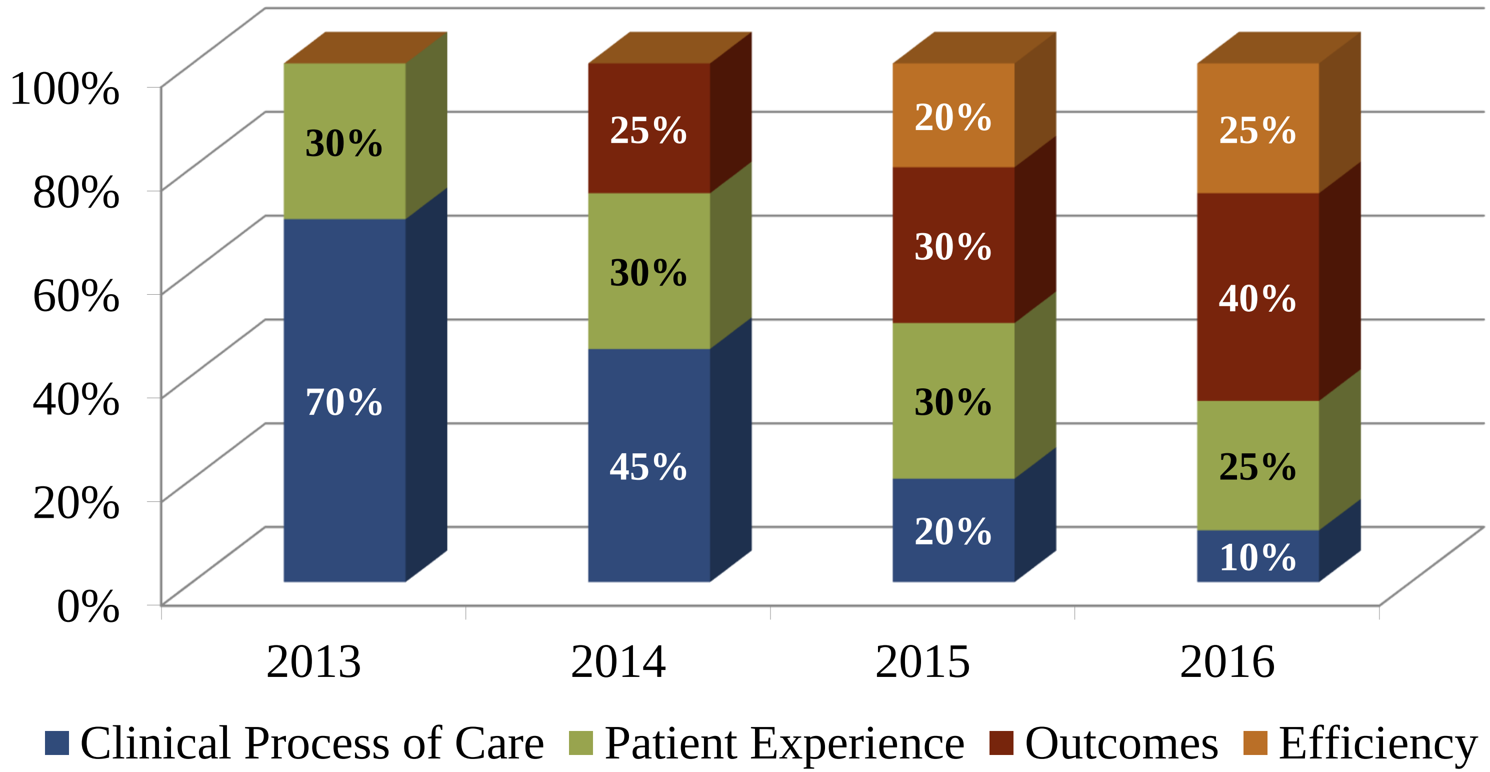
Documenting Value

- 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)

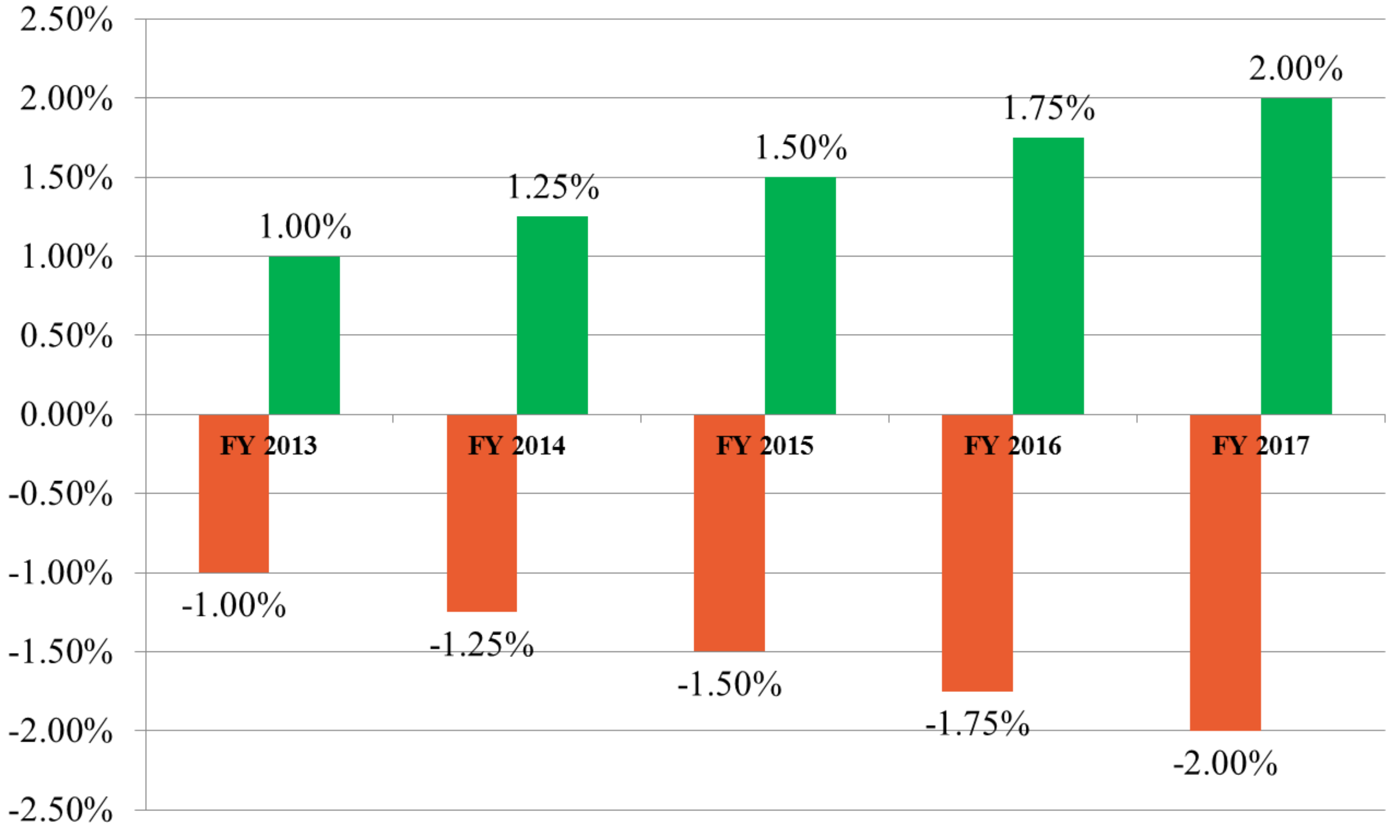
- Adjusts payments to hospitals under the IPPS based on the quality of care they furnish to patients
  - Clinical process of care (timing of tests, interventions, orders, test results)
  - Patient experience of care (HCAHPS)
  - Outcome – (hospital mortality measures for acute MI, heart failure, pneumonia, 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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